

Political equality and global poverty

An alternative egalitarian approach to distributive justice

Abstract:

I argue that existing views in the political equality debate are inadequate. I propose an alternative approach to equality and argue its superiority to the competing approaches. I apply the approach to some issues in global justice relating to global poverty and to the inability of some countries to develop as they would like. In this connection I discuss institutions of international trade, sovereign debt and global reserves and I focus particularly on the WTO, IMF and World Bank.

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by

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*I slept and dreamt that life was joy.
I awoke and saw that life was service.
I acted and behold,
service was
joy.*

- Rabindranath Thakur

The thesis is dedicated to all who expend effort in trying to understand the ways in which unchecked concentrations of power, unequal bargaining power, ideology, propaganda and brute force contribute to human suffering. It is dedicated to those seeking solutions to these ills and to those working to implement these. It is written in the belief that ours is a time of potentially profound social and political changes. It is written in the hope that these changes will include significant moves towards greater justice. Here's to the end of empire, American or otherwise.

Dedication

Personal Note

A highlight of the thesis writing process for me has been the opportunity to read thoughts on a given subject of political concern from a diversity of sources. Issues in global justice, attract the attention of activists in the social justice movements, NGOs (both in the developed and developing countries), scholarly writers outside academia or outside the mainstream of thought in academia, official international institutions such as UNCTAD, as well as academic and mainstream debate in various related disciplines. This opportunity has given me a better appreciation for the place of academic discourse on global political issues within the encompassing sphere of public discourse on politics.

Having been taught by textbook after philosophy textbook that philosophy in the grandest sense is an all encompassing quest for knowledge and wisdom, it is striking to see the ways in which subject matter in a professional discipline like political philosophy might get chosen in practice. It is also striking to wonder how a political philosopher's choice of subject matter might inadvertently shape the rest of political discourse. For all we might say about the fallacy of appeals to authority as a tool in reasoning, it is difficult not to feel that if an issue or idea is not discussed in the academic mainstream, then there is probably something wrong with it.

It has been humbling to gain some inkling of the enormous complexity of social and natural processes and of why people need devote a lifetime to understanding some issues, rather than a mere three years. It has been even more humbling to appreciate the benefits of conducting certain ruminations, unfinished and uncertain as they may be, in public light rather than in private thought or in the privacy of a discipline.

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Chapter 1: Introduction

This thesis is an investigation of the concept of equality in political philosophy. The investigation occurs against the background of an existing literature on egalitarianism. I argue both negative and positive positions. The negative positions include the following. I argue against a focus in egalitarian philosophy on the currency of equality debate, the ‘equality or what’ debate and the intrinsic/instrumental egalitarianism debate. I argue that luck egalitarianism does not accurately capture our understanding of the value of equality. I argue that recent egalitarian literature generally misrepresents the egalitarian perspective on distributive justice.

The positive positions include the following. I describe an account of equality that better matches egalitarian intuitions and that better responds to the conservative opponent. A large part of the thesis is a case study applying this positive account of equality to a set of problems. The problems I investigate revolve around the World Trade Organization, sovereign debt, and the global reserve system, as they relate to development and global poverty. With respect to these institutions, I consider some proposals for egalitarian change by reforming the rules of international trade, creating new mechanisms to manage sovereign debt, and replacing the global reserve system.

1.1 Broadening egalitarian arguments beyond states of persons

I argue that the recent egalitarian literature misunderstands the egalitarian perspective on distributive justice. Distributive justice is concerned with the allocation of the burdens and benefits of economic activity. In investigating egalitarian objections to the distribution of economic product, the existing literature limits itself to considering only objections based directly on the states of persons. I call this the *states-of-persons limitation*. A distribuendum is sought to capture the relevant states-of-persons whose distribution can lead directly to objections to the distribution of economic product. This is the currency of equality debate. The egalitarian literature supposes that an egalitarian perspective on distributive justice means that just distribution of the burdens and benefits of economic activity must depend on achieving the correct distribution (equality, priority, sufficiency) in the distribution of some distribuendum. This leads to the ‘equality or what’ debate and the debate about whether the pattern of distribution is valued intrinsically or instrumentally.

I reject the states-of-persons limitation and propose that the egalitarian approach to distributive justice should be informed by broader egalitarian intuitions. For instance, I contend that one egalitarian reason to object to a given distribution of economic product is that it resulted from unfair institutions. The relevant institutions include not merely economic institutions, but also political, social, and legal ones. Here, the unfairness of the institution, and not any concern about states-of-persons, is the direct reason for the objection. Rejecting the states-of-persons limitation is compatible with allowing that states of persons may still relate to the objection *indirectly*. It seems attractive to think that the unfairness of an institution matters only if it also leads (or could lead) to harmful effects on persons.

Rejecting the states-of-persons limitation casts doubt on the importance of some standard debates in recent egalitarian discussion of distributive justice, such as the currency of equality, ‘equality or what’, and instrumental/intrinsic egalitarianism debates. It also leads to recasting of the importance of the egalitarian patterning

constraint: the view that there exists some good for which an equal distribution is pro tanto distributively just. If egalitarian objections to a distribution of economic product need not be based directly on the states of persons, then it does not seem necessary to give an account of ‘which states of persons matter’, ‘what pattern the states of persons should be distributed’, and ‘whether the pattern matters intrinsically or instrumentally’.

My reasons for rejecting the states-of-persons limitation are these. There are two possible reasons why the egalitarian perspective on distributive justice may be attractive. One, the attraction of the egalitarian perspective on distributive justice may be based solely on the attraction of a distributive pattern of equality for some distribuendum, without relation to the broader value of political equality. I argue that there is no justification for such an egalitarian patterning constraint. In the absence of such a justification, opponents of egalitarianism rightly ask why one should care about a pattern of distribution, in discussing distributive justice. If the egalitarian perspective on distributive justice is based simply on the attraction of a pattern of distribution, then the perspective does not have very wide appeal.

Two, the attraction of an egalitarian perspective on distributive justice may be based on the attraction of political equality, a value that applies not just to distributive justice but also to broader political philosophy. In this case, there is no reason to accept the states-of-persons limitation. Objections to inequalitarian or unfair political and legal institutions can lead to objections to the distribution of economic product determined by the institutions. I argue that such objections are the norm for egalitarian objections regarding the distribution of economic goods.

1.2 The alternative account

My alternative account of equality is based on intuitions and political opinions commonly described as egalitarian. Mine is a *deflationist* account of equality because it does not describe a unique egalitarian political philosophy distinguishable from political progressivism in general. I argue that this accurately represents egalitarian intuitions. Egalitarian intuitions are similar to general progressive intuitions and are too diverse to be bracketed from other progressive intuitions by a substantive underlying theme that unites all and only egalitarian intuitions.

My account also deflates the importance of a distributive justice debate insofar as it is conceived in isolation from the rest of political philosophy. I argue that adequately describing and justifying the egalitarian perspective on just distribution of economic product requires building on concerns identified by an egalitarian perspective in political philosophy more broadly.

I argue that the deflationist account is preferable to luck egalitarianism because it is not susceptible to some of the criticisms levelled at luck egalitarianism, and because it offers a better response to the common conservative opponent. The luck egalitarian account relies on the egalitarian patterning constraint and this constraint cannot be justified. I argue that luck egalitarianism does not match intuitions about certain cases of distribution of economic product. I argue that there are no grounds to suppose that in cases of disagreement with intuition, the intuitions fail to track the value of equality while luck egalitarianism successfully tracks equality. In terms of philosophical utility, I argue that the luck egalitarian account does not play a significant role in identifying the distributive wrongs that concern

egalitarians. Nor is the account necessary to guide egalitarian practical reasoning in constructing solutions to problems that worry egalitarians.

By contrast, my account is not committed to the patterning constraint, and it better matches intuitions about the distribution of economic product. The diversity of values and opinions encompassed by the egalitarian intuitions that motivate my account, means that it can identify a wider range of distributive wrongs that concern egalitarians and can suggest many avenues to pursue in egalitarian practical reasoning.

The luck egalitarian finds common ground with the conservative opponent by emphasizing the importance of choice. She argues against certain distributions of economic product (that the conservative may be happy to defend) by objecting to effects on distribution of factors other than choice. My account finds common ground with the conservative by emphasizing various values in addition to choice, such as fairness, democracy, and non-domination. This allows me to argue objections to certain distributions of economic product because the determinants of the distribution include unfair or undemocratic institutions, or institutions that do not adequately protect the interests of some groups and thus allow them to be dominated. My account allows the egalitarian and the conservative to engage on a wider range of issues.

As for the issues on which the existing egalitarian debate could already engage the conservative, I argue that for many such cases, an inequality in the distribution of some distribuendum co-occurs with objectionable political, legal, or social institutions. For instance, an inability to meet the minimum of adequate nourishment may co-occur with political institutions that do not have adequate consultative or representative procedures to ensure the voices of the marginalised and malnourished are heard. Or, the political institutions may have inadequate safeguards to stop the interests of some group being dominated by the interests of others.

Whereas the luck egalitarian approach to the problem would discuss where the effects of a person's agency end and where the effects of brute luck begin, my account discusses matters that are more tangible. The tangible matters include discussion of an institution's provisions for ensuring the views of affected parties are sought, and its checks and balances to ensure that the interests of one affected group do not unfairly or systematically overpower the interests of others. Institutions are generally open to view, and the egalitarian and the conservative are likely to share common ways of assessing them, such as checks and balances, constitutions, and consulting mechanisms. My account is thus a preferable way to characterise and defend against the conservative an egalitarian perspective on distribution of economic product.

1.3 The need for a case study

Even though my account of egalitarianism is deflationist, it seems that the adjective 'egalitarian' captures some loosely defined but generally understood sorts of opinions and policies in political philosophy. I argue that what unifies egalitarian opinions in this way is not an ideal or ideology. Nor is it a preference for any particular pattern of distribution. Without a unifying substantive ideal, and given the diversity of egalitarian intuitions, it may be difficult to see what characterizes egalitarianism as a tendency in political philosophy.

The way forward is to note the ability to identify progressive views in the absence of a univocal and definitive account of 'progressive' by instead drawing on awareness of the body of work carried out under the label. Similarly, I claim that what

characterizes egalitarianism will be a growing body of work of egalitarian explorations of problems. This will give an indication of the sorts of problems that concern egalitarians and the types of solutions they tend to propose.

I provide some examples of writers and ideas I consider egalitarian. However, perhaps the best way forward is to simply explore some problems from an egalitarian point of view to yield an example of egalitarianism in practice. As an example of how I propose egalitarian philosophy should proceed, I investigate a particular set of problems of concern to egalitarians with the aim of reaching promising proposals for egalitarian change. This case study occupies roughly half of the thesis.

Another reason for this case study is this. In light of my criticisms of the debates that occupy much of recent egalitarian literature (currency of equality, 'equality or what', intrinsic/instrumental egalitarianism), continued research in these fields may not seem as attractive. A deflationist philosophical account of a concept may seem to dissolve the problems that defined the field and thereby threaten to close off further discussion in that field. This is not the case for egalitarianism. Egalitarian philosophers can fruitfully apply their skills in investigations such as the one I undertake, in search of normative prescriptions for change.

Moreover, this suggestion has continuity with some existing work in egalitarian philosophy. Proposals such as the stakeholder society (Ackerman), the Unconditional Basic Income (van Parijs) and compensatory education (Roemer) (see chapter 2, section 2.4) are considered part of the general luck egalitarian outlook. Yet these proposals need not engage the traditional debates about currency and pattern. They can be treated simply as progressive proposals, and assessed against standard criteria for assessing policy proposals such as costs and benefits, and feasibility. Similarly, my case study exemplifies how a philosopher might consider a set of problems and proposed solutions.

1.4 An approach of general prescription for all problems versus an approach of problem-specific prescriptions

Explaining the egalitarian concern over a given issue is, at least *prima facie*, an issue-specific matter. Given the diversity of egalitarian intuitions, there is no presumption that the explanation will apply to all sorts of egalitarian concern on all issues of concern to egalitarians. Related to the absence of a presumption that all egalitarian concerns can be explained in a single way, is the absence of a presumption of a single general prescription for egalitarian improvement. Or rather, there is no presumption of a single prescription that is *useful* or *informative*. This is to be contrasted to relatively trivial prescriptions such as that we should act to bring about a *society of equals*. I contend that there is no reason to retain a presumption that there exists a *general* policy prescription such as a distributive pattern or an ideal description and organization of social institutions which would encompass all plausible egalitarian proposals for alleviating social wrongs.

On my account, the egalitarian approach to making policy proposals for alleviating social wrongs is not via a general prescription. Rather, the egalitarian focuses on a particular social issue and attempts to deal with it specifically. An egalitarian investigation of a social issue would include such tasks as diagnoses of social wrongs, identification of the institutions and agents that contribute to a social wrong under study, assessment of strategies and institutional changes that might alleviate the wrongs and assessment of the costs borne by different groups upon

implementation of possible changes. This sort of investigation is not unique to egalitarianism. It is also recommended by other approaches to political philosophy.

Such an investigation naturally shades into disciplines other than academic philosophy and thus becomes multi-disciplinary. It nonetheless remains *political philosophy* because it seeks normative diagnoses of political wrongs and normative aims and prescriptions for remedial action. Luck egalitarianism, as well as competing political philosophies such as liberalism and Marxism, similarly diagnose social ills and prescribe aims and remedial action.

There are nonetheless differences in how these views and my account undertake the normative tasks. To point out the differences, I overlook the fact that views such as liberalism and Marxism have rich and varied traditions and that the views *qua political philosophy* may not be tidily bracketed from the views *qua* political movements and *qua* multi-disciplinary intellectual endeavours. While this may be unfair to the views, my intention here is not to assess those views themselves, but only to sketch a sharper image of my account. The difference in the normative tasks undertaken by my account and by these other views is this. The latter political philosophies typically diagnose social ills and prescribe remedies via relatively abstract and general prescriptions. Following from my argument that the value of equality is not conducive to such a general diagnosis and prescription without falling into speculation, my account of equality must pursue these same tasks differently. I described above the sort of multi-disciplinary investigation that I believe necessary. This is the sort of investigation I propose egalitarian political philosophers should undertake.

1.5 The choice of a topic for the case study

There are many possible topics for a case study. I choose a topic that is among the more urgent topics of concern to egalitarians, namely, that of global poverty and under-development of poor countries. There are many ways to approach this topic. For example, there are many institutions that determine the global distribution of wealth and the differences in performance of various economies. There are also many actions by many agents and collective agents that determine these things. I focus on a few institutions that affect global poverty and under-development: (i) the rules governing international trade; (ii) the institutions surrounding sovereign debt; and (iii) the global system for managing national reserves. In relation to these, I focus on the World Trade Organization (as the major global body mediating rules of international trade), the International Monetary Fund (as a major mediator in sovereign debt management and as a crucial component of the existing global reserve system), and the World Bank (as another major mediator in sovereign debt management).

For each of (i)-(iii) above, I describe relevant features, their relation to global poverty and development and criticisms. In each case, I consider reforms proposed in the literature (of various disciplines) that would arguably make it easier for poor and developing countries to increase their national incomes and to spend more on poverty alleviation and development projects. The reforms I consider build primarily on works by Thomas Pogge and by economists Andrew Charlton, Bruce Greenwald, Kunibert Raffer, Hans Singer and Joseph Stiglitz. The arguments for the reforms are advanced from an egalitarian perspective. They rest on my account of the sorts of problems that concern egalitarians and of what constitutes an egalitarian improvement in a state of affairs.

To sum up, I propose an alternative understanding of equality. The account incorporates recent insights about the value of equality but does not attempt to define it. I do not prescribe any specific distribution as being particularly egalitarian. I do not describe any specific ordering of social institutions as capturing an egalitarian ideal. While the account is deflationist, it is nonetheless an adequate account of equality. The adequacy of my account lies in its relation to egalitarian opinions about social issues. It explains egalitarian opinions on many social issues. It refuses to speculate beyond what can be supported by our intuitions about equality and consequently refuses to prescribe particular distributions or ideals. It also informs the formulation of egalitarian policy proposals to remedy social wrongs.

1.6 Overview of the contents of the thesis

The thesis is divided into two parts, each containing several chapters. In the first part, occupying chapters 2 to 5, I present my account of equality.

In chapter 2, I describe the main debates in the recent egalitarian literature with which I shall engage. These include the currency of equality debate, the ‘equality or what’ debate, the luck egalitarian approach, and a discussion of how luck egalitarian views are set apart from welfare state liberalism by their radical potential. The currency and ‘equality or what’ debates are revisited in chapter 4. The luck egalitarian approach is discussed in greater depth in chapters 3 and 4.

In chapter 3, I present various criticisms of the luck egalitarian approach. I begin by considering and rejecting several avenues for justifying the egalitarian patterning constraint that is common to luck egalitarianism and to other egalitarian views in the recent literature. I argue that luck egalitarianism does not match our intuitions on distributing economic product. No demonstration is forthcoming that luck egalitarianism accurately describes the egalitarian perspective on distributive justice. In the absence of such a demonstration, I argue that there is not even any particular philosophical utility to supposing that luck egalitarianism captures our understanding of equality *well enough*. Specifically, I consider and reject the possibilities that luck egalitarianism may be particularly philosophically useful by: (i) playing a significant role in identifying the distributive wrongs which concern egalitarians, (ii) providing the uniquely most persuasive response to the conservative opponent and (iii) being indispensable in guiding egalitarian practical reasoning and in construction of practical solutions. These failings of the luck egalitarian approach, the most widely accepted approach in recent egalitarian philosophy, motivate the search for an alternative account of egalitarian distributive justice.

In chapter 4, I present an alternative account of equality based on a list of common intuitions generally acknowledged to be egalitarian. I describe how the intuitions, many of which concern parts of political philosophy other than distributive justice, yield judgments about the distribution of economic product. I argue that the central difference between this alternative approach to egalitarian distributive justice and the existing egalitarian approach is my rejection of the states-of-persons limitation and the accompanying conception of distributive justice as relating to an apt pattern of distribution of some distribuendum. I note that my account connects judgments about the just distribution of economic product to broader political philosophy and thereby erodes the attraction to conceive of distributive justice as a

self-subsistent field bracketed from the rest of political philosophy. I note that my account recasts the importance of some of the debates that commonly occupy egalitarians, such as the currency debate, the ‘equality or what’ debate and the instrumental/intrinsic egalitarian debate. I compare how my account fares against luck egalitarianism in addressing the common conservative opponent and argue that my account is preferable.

In chapter 5, I relate my account to existing views in political philosophy outside distributive justice, and I also introduce my case study. I note that my account does not appear to have an underlying ideology or ideal and is instead problem-based. I note some similarities between my account of egalitarianism and various other positions. I give some examples of the sorts of views an egalitarian might oppose on my account. I describe the sense in which my account is a deflationist account of equality and I defend such an account as attractive. I note that the account is open to either interactional or institutional moral analysis, and note how luck egalitarianism’s focus on circumstances fits in this respect. Then I introduce my case study, explaining the need for it, and the way that it furthers an understanding of my account.

In the second part of the thesis, occupying chapters 6-9, I conduct the case study, separated into three distinct but related discussions.

In chapter 6, I begin by explaining why trade and development are relevant to global poverty and thus to the egalitarian. Then I outline some basics of trade theory and development theory in economics. This theory explains in greater detail some of the mechanisms by which trade can affect income and development. It also serves as the context for the discussion of the World Trade Organization (WTO) in the next chapter.

In chapter 7, I describe various rules implemented by the WTO. I present criticisms of these, based on their effect on the prospects of development and economic growth of developing countries. I consider some wide-ranging reforms of the rules of international trade.

In chapter 8, I outline the institutions surrounding sovereign debt, and describe their relation to global poverty and to development. I present various criticisms of the institutions, based around the fact that they promote accumulation of sovereign debt of poor countries and provide no easy way to renegotiate a debt burden that is unmanageably high. This debt burden affects the prosperity of the poor residents of the indebted country, as well as the country’s chances of development. I propose various reforms that avoid or remedy the problems of the existing institutions.

In chapter 9, I consider the global reserve system. I explain the purposes of reserves and their connection to global poverty. The existing system contributes to global economic instability, making economic crises more likely. Crises can severely affect the incomes of the residents of a country. The existing system also requires poor countries to divert large sums into reserves instead of spending on poverty alleviation programs. I consider an alternate reserve system that avoids the criticisms levelled at the existing system.

Chapter 2: Overview of the recent egalitarian literature

My thesis is an engagement with some recent egalitarian literature. In particular, I investigate the luck egalitarian or liberal equality tradition which dominates that literature. The luck egalitarian (henceforth LE) view is advanced as an understanding of the value of equality in political philosophy. In the first part of the thesis, I criticise that view as an understanding of equality and propose a novel alternative understanding of equality. This chapter outlines some of the main debates in the egalitarian literature, presenting the major options in each debate as well as standard criticisms. It is a scene-setting chapter, familiarizing the reader with parts of the relevant literature which will be discussed in chapters to come. In later chapters, I discuss the various debates in greater detail and advance criticisms which motivate the novel account of equality.

Contemporary debates about equality have focused, for the most part, on issues of distributive equality. Consequently, the first area I consider concerns the question of what ought to be distributed equally. This is the ‘currency of equality’ or ‘equality of what?’ debate. Secondly, I discuss whether philosophers who fall under the broad umbrella of egalitarianism should advocate equality as the pattern of just distribution or some slightly different pattern. This is the equality versus priority debate or the ‘equality or what?’ debate as it is sometimes called. Thirdly, I consider the aim of neutralizing luck as the motivation for egalitarianism. This points to some of the recent work in egalitarian debates which has focused on the injustice of inequalities arising from factors due to brute luck or mere circumstance, as contrasted to factors of ‘option luck’ or voluntary choice. In the final section of the chapter, I consider some proposals for the sorts of policies recommended by luck egalitarian principles. These proposals can be contrasted to other prominent political philosophies such as welfare state liberalism¹.

2.1 The ‘currency of equality’ or ‘equality of what’ debate

An important debate in the literature on egalitarianism concerns the issue of what is to be equalised². I consider the following proposals: preference satisfaction, resources, capabilities and access to advantage.

2.1.1 Preference satisfaction

Let me begin with the view that we ought to equalise preference satisfaction. Proponents of this approach might tout their view by saying that while an equality of resources view (to be discussed below) fetishizes resources in wanting to equalise their distribution, the preference satisfaction approach focuses instead on the distribution of levels of preference satisfaction derived from resources. Some of the criticisms faced by this view relate to *expensive tastes* and to *malformed preferences*.

Consider first the ‘expensive tastes’ objection (Dworkin 1981a: section VIII). In order to equalise the preference satisfaction of two persons, it may be necessary to allocate them different amounts of resources (required to satisfy preferences) if the

¹ There are other important aspects of the egalitarian debate which I omit because they are not relevant to my thesis. For an overview of some others, see for example (Holtug and Lippert-Rasmussen 2007).

² Important works in this debate include the following. (Sen 1980), (Dworkin 1981a), (Dworkin 1981b), (Cohen 1989), (Cohen 1993), (Arneson 1989).

tastes of one are more expensive than those of the other. It seems unfair to give one person a larger share of resources just because she has more expensive tastes.

Now consider the malformed preferences objection³. Consider the example of the contented slave who is so convinced that she has no chance of freedom and that her lot in life is to obey her owner, that she desires nothing but to dutifully carry out the issued commands. It seems unjust to treat this slave as no worse off than others simply because her preferences are satisfied. Intuitively, it seems inadequate to merely equalise her level of preference satisfaction with that of others who do not have malformed preferences and have not resigned themselves to easily fulfilled preferences after convincing themselves that no other preferences will be satisfied.

A distinct approach to equality attempts to answer the ‘expensive tastes’ objection, namely, equality of *opportunity* for preference satisfaction rather than equality of preference satisfaction⁴. According to this view, the equalisandum with whose distribution egalitarians should concern themselves is not preference satisfaction, but rather *opportunity* for preference satisfaction. This approach recognises that the ‘expensive tastes’ objection is only problematic when the expensive tastes are voluntarily acquired. If the taste is involuntarily acquired, the bearer of the taste has fewer opportunities for welfare. The proponent of the equality of opportunity for preference satisfaction view offers such individuals more resources to allow them to reach the same level of preference satisfaction as those who have not been saddled with expensive tastes. A voluntarily acquired expensive taste does not reduce opportunities for preference satisfaction as the agent could choose or cultivate another, less expensive, taste and reach the relevant level of preference satisfaction. This approach cannot be accused of pandering to those with expensive tastes. However, it faces a ‘cheap tastes’ objection. Suppose some individuals require fewer resources than others in order to enjoy the same level of opportunity for preference satisfaction. It might seem unfair to grant them fewer resources just because they happen to have cheaper tastes (Clayton and Williams 2002: 11).

2.1.2 Resources

Some propose that we pursue equality of resources⁵. Proponents of this view might point out that for the purposes of policy-making and implementation, we need a basis for interpersonal comparison that is transparent and based on non-manipulable circumstances of individuals⁶. Individual preferences, as used in the equality of preference satisfaction approach, seem inadequate by these standards. By contrast, the distribution of resources fares well by the standards. However, this proposal is open to the following challenges.

First, it seems unjust that two individuals receive the same amount of resources even though one suffers a costly disability and the other does not. Imagine

³ On adaptive preference formation in general, of which malformed preferences are a variety, see (Elster 1982).

⁴ (Arneson 1989) elaborates an equality of opportunity for welfare view.

⁵ Dworkin proposes a resourcist view in his 1981b. His view is a complex one involving an insurance market as well as an auction in which all have equal purchasing power in bidding for bundles of resources and where the auction stops only when no one wants to change their bid given the bids of others. Such complexities are not discussed in this cursory section on resourcist answers to the currency of equality debate.

⁶ These are, in fact, John Rawls’ reasons for eschewing preference satisfaction accounts in favour of his primary goods approach (Rawls 1996: 181).

an individual who needs a wheelchair to get around. Suppose this individual is given the same amount of resources as someone who is similar to the individual in all ways except that she does not have the need for a wheelchair. Suppose further that the amount of resource distributed is just enough to meet the needs of the second individual and not nearly enough to meet the needs of the individual who requires a wheelchair. Intuition suggests that the person with the greater needs has been treated unjustly in this distribution of resources.

Second, given that we generally value wealth because it is a means to the ultimate end of improving the quality of our lives, surely the ideal distribution of resources should cater to this ultimate end. That is, the concern with resources can be accused of being fetishist, mistaking something that is valuable only as means to a desirable end for being itself an intrinsically desirable end.

2.1.3 Capabilities

Amartya Sen advocates a third approach to the currency of equality issue (Sen 1980). He defines *functionings* as states of being and doing that constitute a person's well-being and that reflect her autonomous ends. *Capabilities* are defined as sets of functionings that the individual is able to achieve given the personal, material and social resources available to her (Anderson 1999: 316). The capabilities approach suggests that particular capabilities should be equalised. Anti-perfectionists might object to this approach on the grounds that picking some capabilities over others relies on a perfectionist view of the individual's well-being. A narrower criticism objects that picking some capabilities rather than others as deserving of state guarantee violates the principle of liberal neutrality between conceptions of the good life (Clayton and Williams 2002: 11-2).

2.1.4 Access to advantage

Gerald Cohen presents a view which can be seen as a refinement of the capabilities approach. He suggests the answer of equality of *access to advantage*. His view has two main components: equality of *access to advantage* rather than of *actual levels* of advantage, and equality of access to *advantage* rather than access to *welfare* or *resources*.

Cohen agrees with Sen that what matters is something intermediate between resources and the utility (in the sense of mental satisfaction) that results from their consumption. The concern with this intermediate stage can be described as a concern for what goods do *to* or *for* people. However, he disagrees with Sen by refusing to call this intermediate good 'capability'. For, capabilities refer to what people are able to do with goods and this is merely a subset of what goods do to or for people (Cohen 1989: 943-4). For instance, one of the things that goods can do for people is to improve their nutritional level. Yet, this is not the same as saying that the person is capable of improving her nutritional level using the goods. Consider an example where a person is comatose and her nutritional level is being improved intravenously. The improvement in nutritional level occurs even though the person, being comatose, is not capable of improving her nutritional level using the goods. This brings Cohen to his concern for *advantage* as a broader term covering what goods do to or for people. Advantage can include mental satisfaction itself, as this latter is one of the things that goods do to people. However, advantage also includes desirable intermediate states between resources and mental satisfaction. These are states of a person caused by the

goods such that the level of mental satisfaction depends partly on the state of the person. The state of being well-nourished is an example of such a state.

Cohen uses the term *access* to include the usual meaning of the word and extends it to include anything that a person actually has. This wider construal of access allows us to consider states of a person that she neither brought about nor ever was in a position to bring about. For example, one has access to the good of freedom-from-malaria if this freedom is due to the fact that others have destroyed all malaria-causing insects (Cohen 1993: 28).

Cohen's position faces some objections also directed at the capabilities view. If equality of access to advantages requires picking out some advantages or states of the individual as being of particular concern to the egalitarian, then the anti-perfectionist can object to this just as she objected to the capabilities account. Similarly, picking some advantages or states of the individual as requiring government intervention can be seen to violate the principle of liberal neutrality between conceptions of the good life.

2.1.5 Concluding the section on the currency of equality

My aim in this section on the currency of equality is not to argue in favour of any particular currency. Nor is it to conclusively fault the various approaches despite the best defences that can be offered on their behalf. I do not demonstrate the strength of the various positions outlined by defending them against the standard objections. Rather, I aim only to outline the main lines along which debate occurs in the currency of equality literature. The main currencies that have been proposed are welfare (of which I have only discussed preference satisfaction variants for constraints of space), resources, capabilities and access to advantage. There is also a debate as to whether actual levels of the currency should be equalised or whether the opportunity for achieving these levels, but not the actual levels themselves, should be equalised (this is reflected in the *access* component of Cohen's access to advantage view).

This ends my survey of the discussion on the currency of equality. Let me move to the second main area of recent debates in egalitarianism.

2.2 The 'Equality or what' debate: equality, sufficiency and priority

The 'equality or what' debate discusses whether egalitarians should pursue equality in the distribution of the relevant good or whether they should instead pursue some pattern of distribution other than equality. Derek Parfit poses the question whether egalitarians should value strict equality of distribution or whether they should advocate only that the interests of the least advantaged be given priority in determining the just distribution. This latter option is known as the Priority view. Thus, the choice Parfit considers is between equality and priority.

Against the strict egalitarian view, Parfit raises the Levelling Down Objection (LDO) (Parfit 1997: 210-1)⁷. Suppose that in a particular case, equality of distribution can only be achieved by making the above average worse off while not making anyone better off. Those egalitarians who favour equal distribution *tout court* would

⁷ See also (Raz 1986: 231) and (Temkin 1993: 247-8) who discuss similar objections to equality of distribution. (Nozick 1974: 229) briefly considers an instance of levelling down in relation to Rawls' Difference Principle.

approve of such redistribution. Yet, it seems counterintuitive to consider the redistribution an improvement even though it is better for no one and worse for some.

A pluralist egalitarian holds that the just distribution is determined by several values, of which equality is only one. Even though the redistribution is an improvement from the standpoint of equality, it is quite the opposite from the standpoint of other values. From the overall standpoint of justice, the redistribution may not be an improvement. Yet, even against the pluralist view, the LDO contends that not only is the redistribution not an *overall* improvement, it does not seem to be an improvement in *any* respect (Parfit 1997: 211). If we follow the intuition behind the LDO, we cannot take strict equality to be a proper aim of justice.

Philosophers who call themselves egalitarians may be divided into two camps as instrumental and non-instrumental egalitarians (Temkin 2002: 129). Non-instrumental egalitarians value an equal distribution intrinsically and not merely for the extent to which it promotes another ideal. Instrumental egalitarians, in Larry Temkin's classification, include some who would not level down in order to achieve an equal distribution. Since instrumental egalitarians do not value an equal distribution intrinsically, they can accept that the redistribution proposed in the LDO is not an improvement in *any* respect. By contrast, the non-instrumental egalitarian values equal distribution intrinsically and asserts that the redistribution proposed by the LDO is an improvement in some respect, though perhaps not an all-things-considered improvement. Non-instrumental egalitarians may be pluralist egalitarians.

Temkin defends non-instrumental egalitarianism by questioning the force of the LDO. He identifies the key premise in the LDO as a 'person-affecting view' that he calls 'the slogan'. The slogan states that one situation cannot be worse than another if there is no one for whom it is worse (Temkin 2002: 132). Let me distinguish theories of good relating to the interests of individuals and theories of good relating to outcomes. The distributive equality debate concerns the justice of outcomes and not merely the good of individuals. The force of the slogan rests on the assumption that the components of the goodness of the outcome include the welfare of individuals and exclude impersonal goods. To illustrate this idea of an impersonal good, Temkin offers the example of proportional justice. The notion of proportional justice assesses outcomes with respect to whether people get what they deserve rather than with respect to whether they are affected for better or worse (Temkin 2002: 139). Temkin's response to the LDO is that equality is an impersonal good. Unless the LDO is accompanied by an argument to the contrary or to the effect that impersonal goods are inadmissible in the debate, the objection is not decisive against the non-instrumental egalitarian.

If Temkin's argument holds, we cannot take the LDO as a decisive argument against non-instrumental egalitarianism and for an instrumental sort of egalitarianism. However, the objection still functions as a thought experiment that persuades us to consider, if not to adopt, instrumental forms of egalitarianism. The priority view is such an alternative.

2.2.1 The priority view

The priority view values equality only instrumentally. The priority view holds that benefiting people matters more the worse off these people are (Parfit 1997: 213). It seeks an equal distribution only to the extent that such a distribution benefits the worse off to the greatest extent possible. Unlike the egalitarian, the prioritarian is

concerned with the absolute level of well-being of the badly off. The priority view does not worry about whether an individual is worse off than others. Accordingly, it does not require levelling down to ensure that no individual is better off than another.

If non-instrumental egalitarianism were the default view, Temkin's stance could be adopted as a bulwark against the LDO in order to resist giving up the default view position. However, one need not begin with non-instrumental egalitarianism as default. The attraction of prioritarianism impresses itself upon us when we instead begin by asking how best to spell out egalitarian intuitions about distributive justice.

Another prominent view in this debate is the *sufficiency* view. Proponents of this view agree with prioritarians that the worse off should have priority, but that there is a threshold level of sufficiency at which the priority ceases. So long as an individual's level of welfare is below this level of sufficient welfare, additions to her welfare have priority over additions to the welfare of the better off. Once the level of sufficient welfare is attained, there is no general reason to prioritise the interests of the worse off over the better off. The intuition behind the view is that, we do not have any concern at all to improve the prospects of the rich as against the very rich, even though the former are worse off than the latter. While there is something appealing about the prioritarian idea of helping the worse off, judging from our intuitions, this appeal disappears if the worse off are already very wealthy. Harry Frankfurt's 1987 and Roger Crisp's 2003 are examples of such a position.

In the debate about how best to spell out the egalitarian intuition with respect to distributive justice, non-instrumental views of equality compete with instrumental ones. The priority and sufficiency views are prominent examples of the latter sort. The LDO has been central to this debate, often referred to as the 'equality or what?' debate.

Let me move on to the third major section of this chapter and discuss the role of luck in recent egalitarian debates.

2.3 The role of luck

Many egalitarians contend that in debates about distributive justice, the guiding question is whether justice requires the individual to bear the cost of various facts about her or whether it allows her to reap the rewards of facts about her. This issue is often captured via a distinction between brute luck and option luck, that is, between circumstance and responsible choice. Views which emphasise this feature are called luck egalitarian. There are reasons why the distribution of wealth can justly be unequal. For luck egalitarians, these reasons are to do with desert. Suppose two otherwise identical individuals expend different amounts of effort. We may say that the one who worked harder deserves more in return for her effort than the other. Justice holds people responsible for such distinguishing factors insofar as it requires the individual to bear their cost or allows them to reap their rewards. These factors, which can justify inequalities in distribution fall under the heading of choice, as opposed to circumstance, or responsibility, as opposed to brute luck⁸. I will generally refer to this important distinction as the choice/circumstance distinction.

⁸ Works discussing the role of luck in recent egalitarian literature include these. (Anderson 1999), (Scheffler 2003), (Kymlicka, 2002: Ch 3). Classic contributions emphasising the role of luck in distributive justice include (Rawls 1971), (Dworkin 1981b), (Arneson 1989), (Cohen 1989) and (Roemer 1998).

I turn now to examine what falls under the heading of circumstance. There are factors that can influence an individual's position in the distribution of wealth over which she has no control. These factors, which may be called matters of brute luck, include both natural circumstances, such as innate talents or handicaps, and social circumstances, such as an individual's upbringing or the social institutions within which she acts. The luck egalitarian approach considers returns from one's circumstances to be undeserved and this leads to the view that justice does not require the individual to bear the cost of bad brute luck and does not entitle the individual to rewards from good brute luck. Given that there is a brute luck factor in the economic position of the talented and the socially privileged, we can justly take away some of their wealth. Given the brute luck factor in the economic position of the disadvantaged and the untalented, such persons should be compensated for their misfortune as a matter of justice.

Though this distinction between choice and circumstance is undoubtedly useful, let me clarify its role in egalitarian debates. The distinction seems to promise a justification for seeking equality in the distribution of one's chosen equalisandum. If we can identify factors beyond individual control which affect the distribution of advantages, then perhaps we can justify a redistribution that neutralizes the effect of these factors.

Against this possible justification for the pursuit of equality, Susan Hurley makes the following criticism (Hurley 2001). To frame her argument, she contends that egalitarianism includes a *patterning constraint* that, for some X, relatively more equal distributions of X are to be preferred to relatively less equal ones, other things being equal. Hurley's point is that the notion of luck can neither justify nor even favour this patterning constraint being advanced as a pro tanto good.

Given the independently specified choice of some good – say, welfare or certain resources – we can use the choice/circumstance distinction to identify those aspects of the distribution of advantages for which the individual is not responsible. So, although the notion of responsibility does not specify the currency of equality, it allows a principled identification of those inequalities in welfare or resources that are due to factors which do not justify inequality and that call out for redistribution in the name of justice.

Hurley points out that if the notion of luck is to ground the egalitarian patterning constraint, it cannot be via the simple path from the claim that it is a matter of luck that A and B (the amounts of the equalisandum attached to individuals X and Y) are unequal to the claim that it would not be a matter of luck if A and B were equal. For, the latter claim does not follow from the former. Perhaps the notion of responsibility can be used to justify departures from a *default* distribution of equality. That is, perhaps we can stipulate that inequalities are allowed only if they arise for reasons for which the individual is responsible. For example, such a reason might be that one individual chose to work harder and longer than another and deserves a proportional return for her greater effort. However, in this case, the egalitarian core lies in the fact that the default position is one of equality. For, we could just as easily stipulate that by default the aristocrat is to have more than the peasant and require that any departure from this state be justified only by concerns of responsibility.

Hurley's essential point is that although the choice/circumstance distinction can help us identify areas where justice requires intervention, it does not tell us which pattern of distribution to pursue in redistribution.

2.4 Ex ante versus ex post ways of effecting egalitarian change

Will Kymlicka conceives of liberal equality as a political vision to be contrasted to other such visions as utilitarianism, libertarianism and Marxism (Kymlicka 2002: ch 3). By liberal equality he means a tradition of thought beginning in Rawls and continuing through Dworkin to Cohen's equality of access to advantage view. He describes the view quite cleanly as involving emphasis on the choice/circumstance distinction. The term luck egalitarianism is used to designate the same sort of view as the term liberal equality.

Kymlicka suggests that liberal equality focuses on redistributing resources or income so as to neutralise the effects of differences in circumstances such as race or gender. Contrast two ways of doing this: *post factum* and *ex ante* redistribution. *Welfare state capitalism* can be described as involving post factum corrections of market inequalities, through taxation and transfer. There can be severe inequality in the initial distribution of physical and human capital as people interact in the market and, partly as a consequence, severe inequalities in the market's allocation of income and resources. The welfare state then redistributes to mitigate the inequalities. *Liberal equality* is more radical in requiring that *all persons start life with an equal share of society's resources*. It aims to reduce inequality in the underlying distribution of property and wealth and to improve equality of opportunity to invest in human capital. The idea is that the operation of the market based on these more equal inputs will generate smaller inequalities (Kymlicka 2002: 88-9 and Krouse and McPherson 1988 quoted therein).

Rawls advocates a "property owning democracy" which involves substantial ex ante redistribution conjoined with a market economy. He expects that this will reduce the need for ex post redistribution and will also reduce various relations of domination and degradation in the division of labour. The view is that liberal equality ought to be concerned not merely with the transfer of income that results from the interactions of people in various social roles, but also with the way in which those roles are defined. It is stressed that important components of the resources available to a person include opportunities for skill development, personal accomplishment and the exercise of responsibility. These matters relate more strongly to social relations entailed by a job rather than to the resulting income. Ex post transfer payments may make the financial condition of the poor more tolerable, but it leaves other aspects of their condition unaltered. For instance, if the poor had a more equal position in negotiation before entering the market, they may not have accepted jobs which entail relations of relative servility to other positions in the division of labour and may have sought a different such division. The division of labour here affects such goods as opportunities for skill development, personal accomplishment and the exercise of responsibility. These are not addressed by mere redistribution of income.

Kymlicka suggests that the recommendations of liberal equality are more radical than the ex post redistribution of income that is generally associated with welfare state capitalism. Liberal equality seeks not only to redistribute income from the advantaged to the disadvantaged, but also to ensure the advantaged are not in a position to define relations of power and servility in the workplace (Kymlicka 2002: 89-90).

Kymlicka takes the views of Ackerman, Van Parijs, and Roemer to be part of the liberal equality tradition (Kymlicka 2002: 95). Their views suggest ways in which

an ex ante redistribution can be undertaken to ensure that all persons start life with the same share of society's resources.

Ackerman proposes a *stakeholder society* in which each person is given a one time, lump sum, payment of money upon graduation from high school. This would reduce considerably the inequality in young people's ability to acquire productive assets or to develop various talents (Ackerman and Alstott: 1999).

Philippe Van Parijs suggests a guaranteed and unconditional basic income (UBI) for all persons in a society. The income differs from Ackerman's proposal partly in that the income is not a large one-time payment, but a lifelong series of regular payments of a much smaller sum (van Parijs: 1991, 1995). Roemer suggests a further variant. Roemer's view, which can be called 'coupon capitalism', proposes that all young adults receive a portfolio of stocks in the nation's firms. A person can trade these stocks at market prices but cannot cash out her portfolio (Roemer: 1994).

Roemer also suggests a model of 'compensatory education'. He acknowledges that equal opportunity for attaining advantages through the market is a desirable goal. However, equal public spending per child in education does not create equal opportunities. Wealthy parents are more likely to value education, to be better educated themselves, and to be willing and able to invest more in their children's education. To equalise opportunity, Roemer proposes *compensatory* education, investing more heavily in poorer children (Roemer: 1999).

Another suggestion by Roemer acknowledges that there is no way to determine the extent to which an individual's disadvantages are due to choice or circumstance. While the luck egalitarian principle of justice may be attractive, it is not immediately clear how it could be rendered practicable. Roemer suggests a way to neutralize the effects of certain circumstantial factors at the social level. Society would construct a list of factors that it considers to be circumstantial. These would include such factors as age, gender, race, disability, economic class or education level of parents and so on. Society is then divided into groups or types based on these, such as '60 year old able bodied black woman whose parents received only primary education' and '60 year old able bodied white male whose parents received tertiary education'. *Within* each type or group, there will be much variety in income and this variety is assumed to result from choice. However, there will be considerable inequality *between* groups or types if we consider the income of, say, the median individual. These inequalities *between* groups are, by hypothesis, circumstantial (Kymlicka 2002: 84-5).

These proposals by Ackerman, van Parijs and Roemer are attempts to neutralise the effects of some circumstances or brute luck factors. A criticism of views that stress the importance of the choice/circumstance distinction and which tie just deserts to choice and not to circumstance is that there is no practical way to isolate the effects of choice from those of circumstance. For example, we cannot isolate parts of a person's talent that have been cultivated by life-long voluntary choice and effort from those that are innate or a factor of the social circumstances in which the person was brought up. The policies of progressive redistribution tied to the welfare state can be seen as ways of mitigating some effects of circumstance on wealth. The views of Ackerman, Van Parijs and Roemer offer more radical, ex ante, approaches to doing the same. They can be seen as attempts to operationalize the choice/circumstance

distinction and make it practicable to roughly distinguish effects of choice and of circumstance⁹.

This concludes the overview of the egalitarian debates with which I engage. In the following chapter, I begin more detailed discussion of some of these debates.

⁹ Views in the left-libertarian debate also contain radical critiques of existing welfare state capitalism. This debate is related to the luck egalitarian approach in that it allows inequalities based on voluntary choice, and re-examines the sorts of brute luck inequalities which should be allowed. Its radical consequences lie in questioning the particular social institutions of returns which attach to various choices and noting that these could, and perhaps should, have been otherwise. A key theme in discussing these institutions is whether natural resources should be seen as initially unowned or as initially collectively owned. This affects the just returns from voluntary use of labour to appropriate or transform natural resources. See the collection (Steiner and Vallentyne 2000) on this debate.

Chapter 3: Luck egalitarianism is not an adequate theory of egalitarian distributive justice

In this chapter, I describe luck egalitarianism in greater detail and assess it as a theory of distributive justice. I argue that it is not an adequate account of the egalitarian approach to distributive justice.

I begin in section 3.1, with a description of the distributive justice debate, and of the general egalitarian approach to it in recent literature. I also describe LE's approach more specifically. In section 3.2, I discuss LE's commitment to the egalitarian patterning constraint and seek justifications for the patterning constraint. I consider three possible justifications and argue that they all fail.

In section 3.3, I assess LE as an account of *egalitarian* distributive justice. This leaves aside the commitment to the patterning constraint, supposing that egalitarians may be happy to accept it without justification. It considers whether LE should be acceptable *to egalitarians* as a view of distributive justice. I argue that there is no reason to suppose it should be acceptable. In section 3.3.1, I note that, in some cases, LE disagrees with our intuitions. In section 3.3.2, I consider a possible defence of LE, that it is a theory of egalitarian distributive justice *per se*, and that, at least in the cases of disagreement, the intuitions are not about this. The defence suggests that in those cases, the intuitions are about more general moral acceptability. I argue that there is no clear reason for judging one way or the other as to whether it captures our understanding of egalitarian distributive justice *per se*.

In section 3.3.3, I consider the possibility that, even if it cannot be *demonstrated* that LE captures our understanding of egalitarian distributive justice *per se*, perhaps there are grounds for thinking that it does. In particular, I consider whether there are grounds based on the philosophical utility of supposing it to be the correct theory. I consider three sorts of philosophical utility the theory could have. I consider (i) whether LE plays a significant role in identifying the distributive wrongs which concern egalitarians, (ii) whether presenting egalitarian concerns in terms of the choice/circumstance distinction is the uniquely most persuasive response to the conservative opponent and (iii) whether it is indispensable in guiding egalitarian practical reasoning and in construction of practical solutions. In each case, I argue that the answer is negative.

Let me set this chapter in context. In the next chapter, chapter 4, I present my alternative account of distributive justice, based in egalitarian intuitions. While I also present in chapter 4 independent grounds for conceiving of egalitarian distributive justice as I propose, this chapter motivates the search for an alternative account of egalitarian distributive justice by noting some shortcomings of LE. The alternative I propose in chapter 4 is not committed to the egalitarian patterning constraint and has a better claim to matching egalitarian intuitions on distributive justice.

3.1 The egalitarian approach to distributive justice

The recent egalitarian debate is in the domain of distributive justice. Distributive justice is the just allocation of the burdens and benefits of economic activity. There are different competing distributive principles that seek to prescribe a certain allocation of the benefits and burdens of economic activity in order to achieve distributive justice.

One proposed distributive principle is that whatever distribution of products of economic activity results from free transactions between people rightfully holding economic goods is a just distribution. This is the position of the economic conservative or the libertarian. A second would be that the aggregate economic product across all persons must be maximised and that whatever distribution is consistent with this is just. A third would be to ensure that all needs are met, and that whatever distribution achieves this is just.

The egalitarian literature has approached the issue of distributive justice in a distinctive way. It has supposed that the just distribution of the burdens and benefits of economic activity is the one which results when the distribution of some distribuendum is equal. The specification of the most apt distribuendum is pursued in the currency of equality debate. The ‘equality or what’ debate investigates whether the apt distribuendum should be distributed equally or in some other way (such as in a way as to prioritise the interests of the worse off).

It is assumed that whatever distribution of economic product the correct egalitarian principle requires, it will require redistribution of the distribution which results from free transactions in the market between people rightfully holding economic goods. That is, the just distribution according to egalitarians will require redistribution away from the just distribution as according to economic conservatives. Egalitarians have taken the economic conservative or right wing libertarian to be a major opponent and have sought to justify egalitarian distributive principles to conservatives.

The luck egalitarian approach notes that the conservative position turns on the importance placed on free, voluntary choice. LE justifies its egalitarian distributive principle to the conservative by incorporating a concern for voluntary choice into its specification of a distribuendum and a pattern of distribution. It might be thought of as a better answer to the conservative opponent because of its incorporation of a concern for choice.

A Luck Egalitarian view is Gerald Cohen’s equality of access to advantage view. Section 2.1.4 of chapter 2 presents a more detailed description of access to advantage and so I do not repeat it here. *Advantage* is a technical term coined by Cohen to include what goods can do to or for people. *Access* includes the usual meaning of the word and Cohen extends it to include anything that a person actually has (Cohen 1993: 28). The *access* component allows a role for choice or responsibility. If an individual has just as much access to advantage as another, but ends up with less because of foolish or irresponsible choices, then the resulting inequality is not unjust. Thus the view incorporates an emphasis on responsibility and choice.

The incorporation of the notion of responsibility certainly makes luck egalitarianism more palatable to the conservative opponent. Nonetheless, the conservative may reject the remaining egalitarian component in luck egalitarianism. Let me explain.

3.2 Egalitarian patterning constraint

The egalitarian approach to distributive justice is commonly taken to assume that there exists some good for which an equal distribution is pro tanto distributively just (Cohen 1989: 906). Let me use the label ‘*egalitarian patterning*

constraint' for this claim¹⁰. I will discuss the constraint with respect to LE in particular.

This patterning constraint appears to be a substantive thesis. A substantive belief is non-trivial, so that accepting it rules out some interesting or plausible alternatives. I investigate how this substantive thesis might be defended. The underlying appeal might be to some proposition such as that (i) the needs, interests and preferences of an individual should receive *equal moral weight*, no matter who the individual; or that (ii) *consistency in practical reasoning* requires that equals should be treated equally and unequals unequally; or (iii), in the case of luck egalitarianism, that the *luck neutrality principle* justifies the constraint. I use some work by Derek Browne to argue that (i) and (ii) are trivial and therefore cannot justify the substantive constraint. With respect to (iii), I use some work by Susan Hurley to argue that the luck neutrality principle cannot justify the constraint.

I begin by saying a little more about the egalitarian patterning constraint and describing the concepts of comparative and non-comparative principles which will be useful in discussing (i) and (ii).

In the egalitarian patterning constraint, the concept of equality is used in the sense of *a relation which holds between any two individuals with respect to any attribute* which they have in common (Browne 1978: 51 uses this characterization of equality). In this characterization, an egalitarian principle of justice would be a *comparative* principle in the sense explained below.

Let us conceive of a principle of justice as a principle which determines what is due to each person in the sense of '*giving to each their due*'. Joel Feinberg distinguishes *comparative* and *non-comparative* principles of justice as different ways in which a principle can determine what is due to any given person (Feinberg 1974: 299ff). Here is an example of a non-comparative principle for determining what is due to each: what is due to each is what is necessary for that person's needs to be met. Here, it is possible in principle to determine what is due to an individual without recourse to the situation of any other. An account based on needs *may* yet use comparisons. Perhaps the account defines certain social needs, for instance. However, other needs-based accounts are possible which make no reference to comparative goods. For instance, the account may include only very basic needs like a threshold amount of caloric intake and a threshold quality of shelter and clothing appropriate to the geographical conditions. While '*clothing appropriate to geographical conditions*' may require some comparison to the usual needs of humans in specific conditions, this is not the sort of comparison in which I am interested. I am interested in interpersonal comparison. So long as there are standards of what is appropriate clothing in specific conditions, no interpersonal comparison is necessary to determine the clothing needs of a person in those conditions.

By comparison, a comparative principle of justice cannot determine what is due to a person without appeal to comparisons to other people. The comparison is logically indelible (Browne 1978: 50). An example is a principle which holds that – given some aggregate amount of distribuendum – what is due to a person is exactly the same amount of distribuendum as that which is due to any other person. Here, one

¹⁰ Susan Hurley uses the label 'egalitarian patterning constraint' to name the equivalent idea (though expressed differently) in her 2001 p2.

cannot determine what is due to a person without comparing her situation to that of another. Let me turn to the first possible justification for the constraint.

3.2.1 Equal moral weight view

Consider the view that the needs, interests, preferences and other morally relevant properties of persons should be given equal moral weight (call it the *equal moral weight view*). It may seem that this belief is necessary to combat *elitism*. If elitism is a real alternative as a principle of justice, then surely the equal moral weight view is morally significant in any principle of justice of which it is a component, as it rules out the elitist option. However, Browne points out that this deals in a straw-man characterisation of elitism, where the latter view is made into a logically incoherent thesis. He argues this as follows.

Values attach to properties, not to the individuals who are the bearers of properties. If persons are individuals who have moral value and pebbles are individuals who do not, this is because of properties of persons not present in pebbles. Attributions of value are necessarily universalizable to all bearers of the relevant property absent relevant differences in context. To characterise the bearer of a property as valuable because of the property and yet deny the value to another bearer of the property simply because the property is instantiated in a *different* individual is unacceptable unless some explanation of a relevant difference in context is given.

If elitism is characterized as advocating this, then the reason for dismissing it is this logical incoherence and not some substantive egalitarian belief. A charitable construal of elitism, rather than a straw-man construal, would maintain that there are morally significant properties which some individuals bear while others do not and that these justify relevantly unequal treatment. The truth or falsity of elitism lies in the moral significance of properties borne by different individuals (a non-relational fact about the individuals) and does not depend on a relational notion of equality (Browne 1978: 57-8). An egalitarian opposing this charitable construal of elitism would argue that no differences in properties borne by different individuals are morally significant in such a way as to justify different distributions of the relevant advantages. The elitist, just as much as the egalitarian, accepts that the relevant attributes of persons must be given equal moral value. They differ in listing the relevant attributes and in prescribing certain dues for certain attributes.

The equal moral weight view is a trivial consequence of the fact that value is attributed to properties, not to individuals, and that attributions of value are necessarily universalizable to all bearers of the relevant property absent relevant differences in context. It is not a substantive thesis which can be characterized as *egalitarian* any more than it can be called elitist. Let us consider a second alternative for defending the patterning constraint.

3.2.2 Consistent practical reasoning view

It might be thought that consistency in practical reasoning requires us to treat equals equally and unequals unequally. Call this the ‘consistent practical reasoning’ view. Yet, just as in the case of the ‘equal moral weight’ view, this formal imperative of practical reasoning is too thin to support a substantive patterning constraint. What it means to treat equals *equally* is a matter differently understood by different theories. Perhaps treating equals equally requires ensuring that each has a fair opportunity to participate in a laissez faire market (which might result in very unequal distributions

of income and various other goods). Perhaps it requires, in part, that the needs of all are met. Given that people differ in their needs, they will require different amounts of goods such as income and various resources. The substantive work lies in describing and defending a theory of what is justly due to each person. It is not clear from the consistent practical reasoning view itself why plausible substantive theories of just dues will entail a pro tanto commitment to the egalitarian patterning constraint.

I have argued that the patterning constraint is not justified by the equal weight view or the consistent practical reasoning view. More generally, it seems that a substantive patterning constraint cannot be supported by a purely trivial or formal imperative to treat equals equally or to give equal moral weight to the interests of all. Let me turn to a more substantive starting point which might be thought capable of supporting the constraint, namely, the Luck Neutrality principle. I argue, expanding on Susan Hurley's argument mentioned above in chapter 2 (section 2.3), that the patterning constraint is not justified by the luck neutrality principle either.

3.2.3 Luck Neutrality

I will use the term 'principle of luck neutrality' (LN) to refer to the principle that inequalities are (i) not unjust if they are the result of voluntary *choices* and (ii) are unjust if they are the result of *circumstances* beyond the control of the individual. Luck egalitarian views place great importance on LN as a pro tanto principle¹¹.

Susan Hurley argues that, while the choice/circumstance distinction can help us identify areas where justice requires intervention, it does not tell us which pattern of distribution to pursue in redistribution (Hurley 2001). Hurley asks which pattern of distribution the luck neutrality principle would prescribe in the case of manna from heaven. Here, the choice/circumstance distinction provides no reason to favour equality of distribution. At issue is not whether some responsible agent should allocate the manna equally or instead according to maximin, but rather whether the LN principle has a preference for either of two situations which both occur as a matter of brute luck. In one situation, by luck, the manna falls from heaven into the laps of people in such a way that it is distributed equally. In another, the manna falls, again as a matter of luck, in such a way as would satisfy the maximin principle.

Hurley points out that the choice/circumstance distinction classifies both cases of manna-fall as matters of brute luck or circumstance. The distinction offers no grounds for preferring the equal distribution over the unequal but maximin distribution. After all, equal distribution of manna is just as much a matter of luck as unequal. The patterning constraint requires that the equal distribution be chosen. This is a distinct assumption not justified by the LN principle.

A related observation which has been made of LE is that, at the a priori level, it is not clear why or whether removing the effects of circumstances on holdings of advantages will move the actual distribution of advantages closer to equality. We cannot rule out a priori the possibility that removing the effects would move the actual distribution *away* from equality. Accordingly, it can be questioned why advocating the LN principle makes a philosopher an *egalitarian*.

¹¹ Scheffler uses these terms to characterise the tendency of Luck Egalitarian views. See (Scheffler 2003: 32).

I am aware of no plausible justification for the patterning constraint. Leaving aside the patterning constraint, let me now consider whether LE is an adequate theory of *egalitarian* distributive justice.

3.3 Assessing luck egalitarianism as an egalitarian account of distributive justice

I investigate whether LE adequately captures our understanding of equality as it relates to distributive justice. I consider two ways in which it might be said to capture our understanding of egalitarian distributive justice. One is by matching our intuitions on egalitarian distributive justice. The second is by matching many, but not all such intuitions, while providing grounds for supposing that it captures our understanding of equality in the remaining cases. In this explanation, it would be our intuition, and not LE, which fails to map egalitarian distributive justice in cases of divergence between LE and intuition.

3.3.1 Luck egalitarianism does not match our intuitions

A comparison between the prescriptions of LN and our intuitions reveals cases of disagreement. There are many cases of brute luck whose effects we do not want to remedy. Samuel Scheffler gives an example of a naturally talented professional athlete who is offered a more lucrative contract than her less talented teammate. The natural talent is a matter of circumstance. Yet, it is counterintuitive to suppose that the difference in remuneration is objectionable simply because of this (Scheffler 2003: 33). It is implausible and counterintuitive to hold that *all* cases of inequality in which circumstance plays a significant role are objectionable. Thus, LE identifies some inequalities as problematic which are not so.

Nor is it clear that people should *bear the distributive consequences* of their choices but not those of their circumstances simply because they are *morally responsible* for the former and not the latter (Scheffler 2005: 12). To see this, consider the following points about voluntary choices. Voluntary choices can be made with varying degrees of skill and deliberation. Practical wisdom – which can roughly be called the skill of choosing well – is affected by various traits of character and temperament. Individuals have different levels of expertise in different spheres of life and cannot generally choose equally wisely in all spheres. To use Scheffler's example, a person who is good at choosing friends may not be good at choosing investments.

Despite this wide range within the class of voluntary choices, it is plausible to suppose that the agent is morally responsible for all voluntary choices. However, it is *not* plausible to suppose that all such choices should be treated the same when we separate those factors whose effects on the situation of an individual we are required to mitigate from those whose effects we are not required to mitigate. We often think it right to alleviate some of the costs of very bad option luck. For instance, there is an intuitive pull to help someone who has chosen unwisely in a field in which she has very little expertise. Though she chose freely within the field, her lack of relevant experience and skill constitutes some reason for helping her. By comparison, if an agent makes a choice in a field in which she has much experience and skill, we are intuitively more comfortable with the idea of letting her cope with the consequences

of the choice¹². Given the different intuitions with respect to whether or not the choice was made with skill, appropriate deliberation, and so on, we have reason to doubt the contention that no inequalities resulting from voluntary choice are unjust.

3.3.2 Intuitions about egalitarian distributive justice *per se* versus all-things-considered intuitions

A defence of LN might urge that the principle captures the notion of egalitarian distributive justice where as the intuition captures an all-things-considered moral judgment. All-things-considered intuitions or judgments involve compromises between all values which are relevant to the case in question. An appropriate balancing of various values may well result in the perspective of equality being overridden by other considerations. The proponent of LN can sympathise with our intuitions and simply say that in those cases other relevant ethical principles outweigh the recommendations of LN. The LN principle might still capture our notion of *egalitarian distributive justice*, but our intuitions in these cases are based on a compromise between the value of equality and other values. Let us assess this strategy.

Consider how one might judge whether LN captures our understanding of egalitarian distributive justice *per se* when it diverges from intuition (which we assume is an ‘all things considered’ intuition). The intuitions which are readily at our disposal are *not* specifically about equality. They are not always specific enough to be compartmentalised according to various values like equality, fairness, justice. We cannot judge whether LN describes our understanding of equality *specifically*, shorn of other moral considerations, by comparing the prescriptions of LN with what our intuitions prescribe. It may seem that we simply have to take the luck egalitarian’s word that her theory *does* capture equality in the cases of disagreement and that the disagreement is caused by our intuitions failing to map equality.

This is not quite the case. The LE account of equality may be preferable if it extends and clarifies whatever vague intuitions we do have about the value of equality in relation to distributive justice. Can we judge whether LE is the correct extension and clarification of our vague intuitions about egalitarian distributive justice?

It is important to bear in mind that LN must not only show that it is preferable to *other principles* (such as the priority or sufficiency views) proposed as extensions of our intuitions about equality. It must also show that doing so is preferable to the default position of supposing that our intuitions about the value of equality *per se* – with no admixture of any other moral concerns - are simply not very precise and are not usefully capable of such extension.

LN correctly identifies many cases as problematic. For example, discrimination based on race, caste, sex and sexuality are wrongs and are identified as problematic by LN insofar as these circumstantial features of humans can cause inequalities in advantages. Yet, as in Scheffler’s ‘talented athlete’ example, LN also identifies some cases as problematic that our intuitions tell us are not problematic.

Based on the cases where LN accords with intuition about equality (for example eschewing discrimination based purely on grounds of sex, race etc), some

¹² Even so, there may be grounds for relieving the costs. See (Fleurbaey 1995) for a view that, it is implausibly harsh for a luck egalitarian view to deem it unjust to socialise the cost to an individual of a bad outcome from a voluntary choice.

philosophers might be happy to suppose that LN also accurately captures the notion of equality in cases where our intuition about equality *per se* (rather than our intuition about ‘all things considered’ moral acceptability) is unclear. Yet, based on the cases of discord with intuitions, other philosophers may refuse to accept that LN accurately describes the value of equality in the cases where our intuition is vague.

I believe that there may be genuine disagreement as to whether LN accurately captures our notion of egalitarian distributive justice *per se* when it diverges from our intuitions (which, at best, map ‘all things considered’ moral acceptability rather than acceptability according to the value of equality alone). I see no grounds for resolving this disagreement except the following.

3.3.3 Philosophical utility of luck egalitarianism as a theory of distributive justice

To judge the acceptability of a particular attempt (such as the LN principle) at describing what the value of equality *per se* requires in distributive justice, we must consider the philosophical utility of supposing equality to be defined by the principle. Thus, the proponent of LN might grant that she cannot establish that LN is the *correct* extension of our vague intuitions about equality in relation to distributive justice. She may contend, however, that LN is the most *useful* such extension and that its utility is sufficient to warrant positing it as a definition of egalitarian distributive justice. The definition would extend to cases where we cannot verify it by appeal to intuitions about the requirements of equality *per se* (rather than the requirements of ‘all things considered’ moral judgment) with respect to distributive justice. I will consider whether the philosophical utility of LN warrants positing the principle as a definition of egalitarian distributive justice.

To do so, I consider (i) whether LN plays a significant role in identifying the distributive wrongs which concern egalitarians, (ii) whether presenting egalitarian concerns in terms of the choice/circumstance distinction is the uniquely most persuasive response to the conservative opponent and (iii) whether it is indispensable in guiding egalitarian practical reasoning and in construction of practical solutions.

If the answer to any of these three questions is affirmative, then there may be reason to think that characterising egalitarianism in terms of LN is *particularly* useful. This may warrant positing LE as what the value of equality *per se* requires in distributive justice. If the answers are negative, we will have to reassess the role and utility of the LN principle. In considering these three questions, therefore, I also clarify the role and limits of the LN principle in egalitarianism.

3.3.3.1 LN does not play a significant role in identifying wrongs which concern the egalitarian

It may seem that the LN principle itself can identify the wrongs which worry egalitarians when it comes to distributive justice, quite independently of pre-existing opinions about the wrongs which concern egalitarians. I argue that this is not the case.

As I noted with respect to Scheffler’s ‘talented athlete’ example, the principle would identify some cases as problematic which are not so. It would also fail to identify cases of egalitarian concern where there is very bad option luck. I again appealed to work by Scheffler in making this point by mentioning different degrees of skill, wisdom and experience with which agents make voluntary choices.

The LN principle and the choice/circumstance distinction (alone) cannot be relied upon to identify cases of concern to egalitarians. Rather, certain sorts of social concerns *preoccupy* luck egalitarians. The preoccupations are based simply on philosophers' political awareness of their society, and on their moral response to the world around them. This is antecedent to any commitment to, or use of, the LN principle. When they discuss the ways in which the LN principle would apply (when they determine which effects of circumstances they should examine) these preoccupations come to mind immediately. As it happens, many of these can be connected by the theme that a choice/circumstance distinction plays an important role. The preoccupations pick out a smaller subset of all the cases identified by LN. That is, not all cases of brute luck inequalities are objectionable. Since the preoccupations select this subset, they (and not LN) identify the wrongs. The cases which preoccupy egalitarians are known to philosophers independently of the LN principle. It is artificial to propose that the philosopher arrives at the concerns *via* the LN principle.

Luck egalitarian philosophers appeal to the principle to explain *why* these existing preoccupations matter to them. In explaining why egalitarians or progressives are concerned over the differential treatment of people based on a feature such as race, luck egalitarians can say that a person's race is out of their control and so should not be something for which they are held responsible. If treatment of a person and their position in the distribution of advantages are properly connected to responsibility, then the differential treatment is unwarranted.

However, there are many sorts of cases which concern egalitarians for which LN does *not* do this explanatory work. An example would be a case of very bad option luck in which someone is unable to meet their basic needs. This is an instance where egalitarians would say that allocation of burdens and benefits of economic activity should be changed to redistribute more benefits to the victim of very bad option luck. The best one can say on behalf of LN is that it explains why a certain problem matters *for some problems, but not for all problems which matter to egalitarians*.

Furthermore, there are other explanations for why other cases of egalitarian concern matter to us. For example, a sufficiency view's emphasis on everyone meeting a basic threshold might explain why a person's misfortune matters to us in a case of very bad option luck. In a case where the richest two percent of the population receive a tax cut instead of greater income distribution to the poorest section of the population (even though the poorest section is mostly able to meet its most basic needs), our concern may be explained as wanting to give greater priority to the interests of the worst off. The sufficiency and priority views as discussed in the egalitarian literature may not explain why *all* problems which matter to the egalitarian do matter, but that is also the case for LN.

3.3.3.2 The effectiveness of LN against the responsibility-based conservative

It is not only that the different principles (LN, priority and sufficiency) explain the significance of different problems for the egalitarian. In some cases, the significance of the self-same problem can be explained in more than one way. Consider egalitarian concern over global poverty. There are many reasons that this issue matters. One, the global poor are extremely poor – lacking secure access to the satisfiers of basic needs such as adequate nutrition and shelter. They are either below

or perilously close to any plausible *sufficiency threshold* one may draw. Two, it can be argued that various international institutions effectively prioritise the interests of the global rich over the interests of the global poor. Indeed, I will argue this in the later half of the thesis. This suggests that the status quo is a far cry from the ideal situation according to a *priority view*. Three, the advantages and disadvantages allocated to individuals globally is correlated with their country of birth and the political history of the country over the last few centuries. Global inequalities in advantages are dependent on these *circumstances*.

Yet, it might be thought that casting the significance of such issues in terms of LN is preferable to casting it in terms of, say, a failure to meet the basic needs of some persons or the failure to adequately prioritise the interests of the worst off. A reason for thinking this is the possibility that LN is *strategically* the most useful explanation of why these problems matter to egalitarians.

It has been noted that LN is a particularly persuasive response to the responsibility-based conservative. For egalitarians engaging in debates with conservatives, this is a strategic point in favour of LN. A prominent conservative theme is an emphasis on responsibility for one's lot as a reason against redistributive intervention in the lot that people have procured for themselves. Kymlicka, among others, notes that luck egalitarianism cleverly makes use of the same principle of responsibility so dear to these conservatives. It argues for limits to the market (as well as ex ante changes) to neutralize effects of factors for which the individual is *not* responsible (Kymlicka 2002: 88).

It is true that the LN formulation is a strong egalitarian rejoinder to conservatives in some cases. It is therefore attractive on many issues to cast the disagreement with the conservative in terms of responsibility and LN. However, not all disagreement between the egalitarian and the conservative hinges on the issue of responsibility. Accordingly, it is not clear why LN should be thought to be the most strategic presentation of egalitarian concern *as a default*. How best to present to the conservative the reasons for egalitarian concern, should depend on the issue being debated. Sometimes, couching the disagreement with the conservative in terms of responsibility and LN will not be the most helpful path¹³.

As an example, consider once again the problem of abject poverty throughout the world, and the related desire of poor and developing countries to develop. It is not a popular conservative rejoinder on this issue to say that the developing countries or their citizens are poor because of their voluntary choices.

Some common rejoinders from conservatives in the developed countries are nationalistic – not wanting to cede power or wealth – though others are not. The conservative will likely agree that the inequalities are not due entirely to the voluntary choices of individuals among the global poor or of collective agents such as developing country governments. They will likely agree that the inequalities are due in part to factors like colonialism and to more recent history of military and political

¹³ In the next paragraph I consider examples related to the case study I undertake in the second part of the thesis. Let me also mention in passing the left-libertarian debate with the economically conservative libertarian. That debate is framed around the *fairness* of considering natural resources to be initially unowned. The conservative sees them as such, and derives the consequence that all of the returns from voluntary effort to transform such resources rightly belong only to the labourer. Left-libertarians note that if the resources are viewed as initially collectively owned, not all of the returns from the labour may rightly belong to the labourer. See (Steiner and Vallentyne 2000) for examples of this literature.

interventions by developed countries and protectionism by developed countries in international trade. The conservative might agree that the situation needs to be remedied. She simply disagrees with the progressive about the way to remedy this. For example, the conservative might propose completely free international trade, whereas her opponent might propose otherwise. The conservative may also wish to introduce other values such as fairness in debating the progressive. Fairness may be invoked to demand that all countries should follow the same rules (which conservatives may argue ought to be rules of free trade), rather than allowing preferential treatment for poor countries.

One can perhaps characterise the egalitarian concern for this problem in terms of the brute luck of being in a developing country. However, one can also characterise the matter differently. Indeed, the most immediate reason why the issue captures the sympathies of developed world residents is probably the abject poverty and the unmet need reported from the developing world and the relative affluence of the West which translates to the suspicion that the interests of the worst off are not adequately prioritised.

In any case, since the popular conservative stances on the issue do not include an insistence that the situation of the developing countries is of their own making, it is not particularly interesting to cast egalitarian concern for the issue in terms of LN or in terms of responsibility. It seems more relevant to try to weaken the nationalistic impulse in favour of a cosmopolitan one by emphasising the seriousness of the poverty and unmet needs amongst the abject poor, and to contrast this to the affluence and relative security of developed countries. Or it may be necessary to point out that estimates of the cost to the developed world of progressive policy which helps the developing world is such that it can be absorbed by the former. Or one can emphasise the unfairness of the developed countries having used particular policies in attaining their industrial might, while now denying those same policies to the developing countries (and thus kicking away the ladder, as it were). Or one can make attributions of responsibility for reasons other than LN. For example, Pogge 2005 mentions the responsibility of developed country governments in maintaining the unjust global institutional order. This attribution of responsibility would not serve the same purpose as LE's discussion of the responsibility/brute luck distinction. It aims to motivate citizens and governments of developed countries to see their connection to global poverty not as one of potential benevolent charity for a situation of someone else's making, but of responsibility for the perpetuation of inequality and of the poverty of others.

Some conservatives share the desire to improve the lot of the abject poor and of developing countries generally, but disagree with progressives on the means to this end. In these cases, it is irrelevant whether the egalitarian position is cast in terms of unmet needs, or the choice/circumstance distinction, or oppression, or fairness. What is relevant is empirical debate on the best means to alleviate the poverty and to ease development. In the later half of the thesis, I will engage in just this sort of empirical investigation and construct an egalitarian proposal for change.

Egalitarian concern over an issue can often be explained in more than one way, perhaps by the choice/circumstance distinction or in terms of unmet need. I contend that the choice of one of these explanations over others should be determined by what seems to be the main concern on a given issue, and by what would be most effective against the conservative position on a given issue. There is no reason to

think that the LN explanation should be paramount. Consequently, this is not a reason for thinking of LE as strategically the best account of egalitarian distributive justice.

3.3.3.3 LN principle plays no indispensable role in guiding practical political reasoning for egalitarians

It might be thought that the LN understanding of egalitarian concern is particularly attractive because it guides practical political reasoning and helps in the construction of potential solutions. I argue that the LN principle does not play a key role in guiding practical political reasoning on issues of egalitarian concern.

Consider the relation of the LN principle to practical reasoning. The principle of luck neutrality is a very abstract one. In order to guide practical reasoning, such as by making policy recommendations, a luck egalitarian view must first specify certain sorts of advantages of society which it claims are important and on which it wants to focus. It must specify important ways in which these advantages are determined by factors beyond an individual's control. It must choose certain sorts of factors on which to focus. It must describe ways of measuring or approximating the effects of various circumstances.

Yet these steps do not have a significant role for the LN principle itself and have been common aids to political practical reasoning quite independently of LE. These steps of practical egalitarian reasoning rely on philosophers' *already existing preoccupations* with certain sorts of issues and on *politics* as a way of adding to this list of issues.

The *preoccupations* include awareness of phenomena like malnutrition in society (adequate nutrition being an advantage). They include awareness of possible contributors to malnutrition such as improper functioning of markets, political instability, corruption, poverty, political marginalization of the affected group, and lack of adequate safety nets. They include an understanding of which sorts of factors it is most useful to focus on. For instance, while both drought and lack of adequate safety nets are possible contributors to famine and malnutrition, it is likely more useful to focus on the safety nets rather than on drought.

Politics can add to the debate in many ways including through social movements, representative politics and democratic consultation with citizens about issues of concern to them. These means continually bring to light unmet needs, inadequate consideration of the interests of marginalised groups, discrimination of various sorts and so on.

Nonetheless, the LN principle or the choice/circumstance distinction can be made to guide practical reasoning in some ways. A proposal by Roemer is an example.

Roemer acknowledges that there is no way of determining the extent to which any individual's disadvantages are due to choice or circumstance (Roemer 1998: ch 2). Roemer's theory of the egalitarian planner suggests a way to make LN relevant to politics. In a sense, it operationalizes the choice/circumstance distinction. He suggests that democratic deliberation and negotiation should determine a set of factors which society considers to have significant effect on individuals' situations and which are outside of the individual's voluntary control. These factors would likely include things like age, gender, race, level of education of parents and so on. Society is then divided into groups or types based on these, yielding groups such as '60 yr old able

bodied black woman whose parents received only primary education'. Within each type or group, there will be much variety in income. We assume that this variety results from choice. The inequalities *between* groups are, by hypothesis, circumstantial. So, the inequality between the median incomes of the group '60 yr old able bodied black woman whose parents received only primary education' and the group '60 yr old able bodied white man whose parents received tertiary education' are assumed to be circumstantial. Redistribution can be effected to ensure that the circumstantial inequalities do not exist, while the inequalities within each group may remain.

Here, the choice/circumstance distinction guides practical reasoning by providing a framework whereby to discuss acceptable and unacceptable differences in holdings of wealth and resources. The LN principle characterises the general aim of the proposal. The choice/circumstance distinction structures the question posed to the population in the deliberative process. For instance, the question may ask: which factors do you think are (i) mere *circumstance*, (ii) have significant effects on income and resource distribution and (iii) should not be the cause of *differences* in these distributions? The question is answered through politics. It depends on people's considered opinions which are themselves coloured by other factors such as the visibility and effectiveness of social movements.

However, much practical egalitarian thinking can proceed *without* appeal to the principle. The principle is not necessary. Egalitarians can simply pick out one of the many issues of concern to social movements and research the best way to deal with it. I will do just this later in the thesis. Or, if they want a guiding question or framework – something which the LN principle and the choice/circumstance distinction provide – other such questions are at hand. For example, egalitarians can ask: which are the basic needs which everyone should be able to meet? Or, which laws or institutions treat people unequally in significant ways? Or, which laws or institutions serve to perpetuate inequalities in important goods such as the level of education or wealth or job opportunities or land ownership over generations or over a lifetime? Or which global economic features and institutions hinder the ability of developing countries to diversify their economies and raise national incomes?

The answers to the three questions posed at the start of section 3.3.3 have been negative. There is no reason to think that characterising egalitarian distributive justice in terms of LN is *particularly* useful. There is insufficient reason to suppose that one can describe what egalitarian distributive justice *per se* requires uniquely in terms of the LN principle.

In this chapter, I have given grounds for being dissatisfied with LE both for its inability to justify the egalitarian patterning constraint to non-egalitarians, and for its dubious claim to capturing egalitarian intuitions about distributive justice. In the next chapter, I present an alternative account of equality which is not committed to the egalitarian patterning constraint and which has a better claim to matching egalitarian intuitions on distributive justice.

Chapter 4: An alternative account of egalitarian distributive justice

In this chapter, I describe a new egalitarian approach to distributive justice. The account begins by listing some egalitarian intuitions, egalitarian concerns and egalitarian political opinions. Based on the list, I present reasons why egalitarians might object to allocations of the burdens and benefits of economic activity. This constitutes the basic egalitarian approach to distributive justice. This is carried out in sections 4.1 and 4.2.

The crucial difference between the resulting alternative account of egalitarian distributive justice and the existing egalitarian literature on distributive justice is this. In investigating egalitarian objections to the distribution of economic product, the existing literature limits itself to considering only objections based on the states of persons. I reject this limitation because it is not suggested by egalitarian intuitions. This has consequences for the existing egalitarian literature. For example, some of the major debates in the literature – such as the currency of equality debate, the ‘equality or what’ debate and the intrinsic/instrumental egalitarianism debate – flow from the acceptance of this limitation. Once the limitation is rejected, this calls into question the importance placed on those debates in the egalitarian literature. This is discussed in section 4.3.

In section 4.3.1, I note that rejecting the states-of-persons limitation and adopting the broader account of equality I propose makes it unhelpful to consider distributive justice as a relatively self-contained debate. Worries about the distribution of the burdens and benefits of economic activity should be considered in relation to broader concerns in political philosophy which have not generally been emphasized in the recent egalitarian approach to distributive justice. I consider and reject grounds for retaining the limitation in section 4.3.2. Doing so leads into the discussion in section 4.4.

In section 4.4, I compare my account to LE by relating them to the common set of problems they set out to solve. While LE has been touted as particularly adept at justifying to the conservative the egalitarian opinions about distribution of economic product, I argue that my account does a better job.

4.1 What are egalitarian concerns, opinions and intuitions?

Some of the egalitarian intuitions other than those used in LE are familiar from other parts of the egalitarian literature. The priority view emphasizes the intuitive attraction towards the view that the interests of the least advantaged in society ought to have a disproportionate pull on us. The sufficiency view emphasizes the importance of ensuring that all members of society are provided with some threshold level of the important advantages of society.

The domain of egalitarian concerns, intuitions and opinions would include concerns about wealth inequality within a country or globally; differential treatment of people based on their race, caste, gender, sexuality or ethnicity; the extent and depth of global poverty expressed in terms such as access to education, healthcare, adequate nutrition, shelter; the subjugation of populations to an elite or a despot; the greater effective access of special interest groups to policy makers; domination of one group of individuals over another; uneven bargaining power in the drawing of a

contract or in the design of an institution; systematically uneven distributions of returns from a scheme of mutual cooperation (without adequate consent of the disadvantaged); poor checks and balances on political or civic institutions allowing decision makers to systematically favour one group of interests over another; unrepresentative decision-making by governing bodies enabled by absence of requirements to perform adequate consultation, and so on.

Egalitarians would commonly want to eliminate such discrimination, reduce wealth inequality, improve access of the global poor to basic goods such as adequate nutrition, shelter, healthcare and education, release subject populations from control of an elite, improve access of citizens to policy makers relative to corporations, reform institutions more fairly, design checks against unfair contracts, and introduce checks and balances into governing bodies.

These political opinions can be described as egalitarian. These opinions may also be shared by people who would not label themselves egalitarians. Many progressives and liberals might share these concerns. This is not problematic, as my intention is not to describe a set of views unique to egalitarianism, but to describe a set of views which are emblematic of egalitarian concern.

The set of *values* commonly invoked by egalitarians in describing egalitarian concerns does not stop at equality. The fact that values other than equality often figure alongside the value of equality when egalitarians describe some of their concerns is not a reason to strike these concerns from the list of egalitarian concerns. The intention in drawing this list is to give an indication of concerns which are commonly thought of as egalitarian, not of concerns which are commonly thought of as having to do with the value of equality *and no other*. Such values which figure alongside equality in egalitarian opinions include democracy, self determination, fairness, meeting basic needs, protecting basic liberties.

The egalitarian literature on distributive justice has appealed to some of the intuitions listed. For example: whether we are concerned merely about income or also about nutrition levels and access to healthcare; whether we should help those who have substantially less than others even if the first group can meet all of their basic needs; whether a preference for prioritising the interests of the worst off in comparisons of the abject poor and the most wealthy extends also to cases where the inequality is smaller; whether it is mere inequality of wealth which bothers us or rather the extent or cause or type of the poverty of some group.

Note that the diversity of the values invoked, the diversity of subject matter (including political, social, economic and legal institutions), and the similarity of the views to progressive views in general, give reasons to suppose that no single substantive notion of equality underlies all of these concerns. Perhaps a common thread is to be sought which connects the various insights in the recent egalitarian literature, as well as other egalitarian intuitions such as those regarding fairness. This connecting thread would be a more promising candidate for the proper account of equality. I am aware of no plausible and informative common feature. The common features which spring to mind as potential candidates are the formal principles of the 'equal moral weight' view and the 'consistent practical reasoning' view considered in sections 3.1.1 and 3.1.2. These *formal* principles are surely important, but their importance does not extend to furnishing *substantive* political prescriptions as we might expect from an egalitarian political philosophy. By themselves, the two views are simply formal imperatives on practical reasoning followed broadly across the

political spectrum rather than specifically by egalitarians. In section 5.1.4 of chapter 5, I add to this point about the absence of a substantive unifying theme that connects egalitarian intuitions.

4.2 Applying the egalitarian intuitions to distributive justice

Some of the egalitarian intuitions above relate to states of persons independently of the broader social context. For example, there are egalitarian concerns about the inability to meet basic needs of a person in abject poverty. Here the distribution of economic product can be of egalitarian concern independently of the cause of the poverty of the individual, simply because of the absolute level of well being of the individual.

However, other egalitarian intuitions relate to concerns of political philosophy considered broadly. Political equality relates to issues about basic liberties, self-determination, constitutional protections and checks and balances against certain actions by government, the fairness of major political, economic and civic institutions, the balance of the interests of agents in various roles defined by an institution, the existence of institutions (such as news media and public education) to help citizens make informed decisions about government and about other powerful agents such as corporations, and so on. These concerns are not related to states of persons, but rather to the nature of institutions within which persons act. These concerns are important independently of their effects on distribution of economic product. They are commonly discussed in political philosophy for their intrinsic importance, quite independently of effects on distribution. However, they also affect this distribution and the distribution can be questionable because they result from unfair causes. It is thus that these broadly political concerns of egalitarians determine an egalitarian position on distributive justice.

The egalitarian intuitions yield many reasons to object to a given distribution of economic product. Scanlon has noted a few ways that some inequalities in distribution of economic product can have objectionable *effects*. Because of such objectionable effects, egalitarians may advocate compensating redistribution of the economic product. Inequalities can give some people an unacceptable amount of control over the lives of others. Debates surrounding campaign financing law discuss ways to limit the objectionable effect of grossly unequal allocations of disposable income on electoral politics. More generally, the fairness of certain institutions may be undermined because of large inequalities in the wealth of the participants in the institution (Scanlon 2002: 44). The priority and sufficiency views also present familiar egalitarian reasons for redistribution. The economic product allocated to one individual may be insufficient to allow her to meet her basic needs, or the inequality of distribution might reflect that the interests of the worse off are not adequately prioritised.

The distribution of economic product may also be objectionable because of the *causes* of the distribution. LE acknowledges the relevance of some causes, based on whether the cause was voluntary choice or brute luck. However, the egalitarian intuitions listed above also suggest the following. There may be an egalitarian case for redistribution if the distribution is unfair. The parties to a contract which led to the distribution may have had uneven bargaining power or the contract may have been made under conditions of asymmetric information available to the contractors. A

distribution may be objectionable because some of the individuals involved had insufficient say in the design or running of the background institutions which significantly affect distribution, perhaps because free transactions occur within the context of these institutions. Note that these institutions include not merely the main political or economic institutions, but also legal and civic institutions that either contribute to the existing distribution or that give rise to compensation claims most reasonably implemented in terms of economic product. A distribution may be objectionable because the major social institutions allow one group to dominate other groups in society. That is, the first group might make decisions in the major social institutions which affect the second group without due consideration of the interests of the second group. These institutions can affect the allocation of economic product.

4.2.1 The relation of non-economic institutions to economic burdens and benefits

To emphasise the point that broader political concerns can motivate objections to the distribution of economic product, let me clarify that the broader political concerns are not restricted to economic institutions. They span political, legal, and civic institutions as well. Consider egalitarian concern over a case of the abject poverty of an individual. The egalitarian may recommend remedial action that involves immediate redistribution of economic product as well as institutional reform. The institutional reform is recommended for such reasons as that some institutions may be unfair, or there may be inadequate mechanisms to ensure the interests of all affected by an institution are given due consideration. Let me list a few of the institutions that set the context for the economic activity.

A government may undertake public good projects such as building essential infrastructure to spur certain types of entrepreneurship. It may run certain industries publicly or semi-publicly in market failure cases such as natural monopoly. It may attract business to particular areas by offering concessions such as subsidies on land lease or on inputs like electricity and water. There are various grounds for government intervention to fix market failures, improve efficiency, and to promote economic growth or development. These and other economic grounds for government intervention will be discussed in chapter 6.

Laws and regulations, including those set by branches of government, define what can be done with various sorts of property. Intellectual property rights are a hotly discussed example. Laws define what constitutes breach of copyright; what constitutes an innovation worthy of a patent or of a distinct patent; how patented properties may be used, and so on. The left-libertarian debate also discusses legal definitions of property. It scrutinizes the Lockean proviso that natural resources can be appropriated so long as 'enough and as good' is left for others, and considers the repercussions that follow from assuming that natural resources are initially unowned (see for example, Steiner and Vallentyne 2000). Regulations define the type of burden of proof an entrepreneur or a government entity must meet before being allowed to carry out a project. For example, private and public entities undertaking certain sorts of enterprises may be required to consult affected populations to a stipulated degree, to address their concerns in certain ways, and otherwise establish that the costs of a proposed enterprise, for groups of individuals and to society at large, are not too great.

Political institutions affect how governments make many of these decisions. Politicians may be lobbied or bribed, or they may inadequately weigh up the costs and benefits of a decision. Political and bureaucratic institutions define and monitor

political lobbying and corruption and set standards for transparency in decision-making. The effectiveness of news media institutions at reporting on government body decision-making is also relevant to whether the decisions reflect the interests of the general public, as opposed to the interests of well-resourced special interests groups who make an effort to remain informed on the decision-making process. For more on special interest groups, see chapter 6.

4.3 Re-conceiving the distributive justice debate

The crucial difference between my account and the existing egalitarian literature lies in rejecting the implicit limit that egalitarian accounts of distributive justice must deal only in states of persons. The existing literature assumes that an egalitarian position on distributive justice must specify some *distribuendum* which is to be distributed equally. *Distribuendums* are states of persons. Thus, in investigating egalitarian objections to the distribution of economic product, the existing literature limits itself to objections relating to states of the persons involved in the distribution of economic product. I will refer to this limitation as the *states-of-persons limitation*. My account rejects the states-of-persons limitation. It investigates egalitarian objections to the distribution of economic product that are based not only on states of persons, but also on objectionable institutions within which the economic product is determined.

Note that institutions are objectionable because they affect (or can affect) states of persons. To reject the states-of-persons limitation is not to suppose that institutions are objectionable even if they have no bad effects on people. It is to say instead that objections to a distribution of economic product need not be based *directly* on how these affect states of persons. They may be based *directly* on the institutions that determine the allocation of economic product. In this latter case, the objection to the distribution of economic product may be *indirectly* related to states of persons, as the unfairness of an institution may be thought to matter only if the unfairness has (or could have) harmful effects on the states of persons.

Given the states-of-persons limitation, it seems natural to carry out philosophical discussion in the tradition of discussing an apt *metric of welfare*, spanning such metrics as utility, preference satisfaction, capabilities, midfare, and advantage. In the metric of welfare discussion, it seems natural to pose such questions as: ‘what is the apt metric?’ (currency of equality debate); what ‘is the most apt pattern of distribution for the metric?’ (‘equality or what’ debate); and ‘is the most apt pattern valuable intrinsically or instrumentally?’ (the debate between intrinsic and instrumental egalitarians). Rejecting the limitation to states of persons recasts the philosophical importance of the debates that have dominated recent egalitarian literature. If egalitarian objections to a distribution of economic product need not be based directly on the states of persons, then it does not seem necessary to give an account of which states of persons matter, what pattern the states of persons should be distributed, and whether the pattern matters intrinsically or instrumentally.

Concern about the justice of a distribution of economic product can be caused by an assessment of the process that led to it. Egalitarian intuitions about the justice of a distribution of economic product can be based on concerns about political, legal, economic and other social institutions. They need not be based on concern about the states of a person. This connects broader political philosophy (which deals with such institutions) to distributive justice. This leads to a questioning of the usefulness for egalitarians of parsing a distributive justice debate as a subset of broader political

philosophy. The alternative I advocate is to discuss egalitarian concerns, including the concern for distributions of economic product, in political philosophy broadly.

4.3.1 Connecting distributive justice and broader political philosophy

The distributive justice debate is about the justice of the distribution of economic product. There is no reason to suppose that the only moral concerns relevant to judging the justice of this distribution are concerns related to the states of individuals. States of persons are certainly relevant, as is clear in the egalitarian intuitions about the ability of a person to meet basic needs. However, it is also relevant to consider the nature of institutions which contribute to the generation of the economic product. Indeed, the conservative, or free market libertarian position, on distributive justice (described below in section 4.4.1) already makes institutional matters important.

What then, is the use to egalitarians of carrying on the distributive justice debate independently of the rest of political philosophy? Consider cases in which egalitarian intuition relates to the state of the individual alone. This would be because the basic needs or the non-basic needs relative to her society are not being met. Or it might be because the level of inequality across a society, in the distribution of certain states of persons, suggests that the interests of the worse are not being given adequate priority.

However, in many cases where needs are not being met or there is inadequate priority, institutional matters will also be relevant. For instance, it may be that the worse off individuals are marginalised in the political process and their interests receive inadequate representation or consideration in policy-making.

There may be some cases where the states of individuals are relevant to egalitarian concern and there is *no corresponding egalitarian concern over institutions*. I would conjecture that such cases of genuine concern would be relatively rare. The bulk of cases where egalitarians are unhappy with the distribution of economic product will be cases where there is related concern about whether the design and function of relevant institutions treats people as equals.

Generally, particular problems relating to distributive justice will also relate to broader debates in political philosophy. In a few cases of egalitarian concern about an individual's holdings of economic product, there may be no relation to broader political philosophy. All relevant institutions may function blamelessly, yet a person may be in very poor shape, perhaps because of very bad option luck or just plain foolish and irresponsible decisions. These cases may well be 'hard cases' for egalitarian political philosophy. Unlike the other cases, where concerns like fairness and representation and checks and balances can be used as common ground to engage the conservative, these cases offer no common ground. However, I see no reason to see hard cases as particularly *representative* of the egalitarian approach to political philosophy. Instead, I suggest that more common cases of egalitarian concern should be taken as representative.

Nor is it clear that pursuing these hard cases will reveal the '*essence*' of the egalitarian approach to political philosophy in a way that investigating other cases would not. These hard cases of egalitarian concern are just some among many other cases of egalitarian concern. There is a diversity of types of concern which are called 'egalitarian'. Some relate to states of persons, while others relate to the nature of

institutions. More than one type of concern can attach to the same instance of concern and in such cases, one type of concern can be offset by another. If an egalitarian wishes to argue that, (i) contrary to appearance, a single essence of equality underlies these diverse intuitions, and that (ii) this essence is better revealed by hard cases than by representative cases, then I contend that the burden of proof is on this egalitarian.

As I have argued above, to represent the egalitarian position in general and to contrast it to the conservative position on the distribution of economic product, one need not focus on states of an individual. I propose that egalitarians should focus on matters of broader political philosophy. This makes dubious the usefulness of a distinct egalitarian position on distributive justice (rather than in political philosophy). I argue against the bracketing of egalitarian philosophy within a niche of distributive justice.

4.3.2 Is there a reason to retain the states-of-persons limitation?

It might be thought that there are benefits to retaining the states-of-persons limitation. It might be thought that ideally, philosophical discussion about politics should be grounded in the states of persons. The rationale for this view might be that only these are capable of bearing intrinsic value. If things other than states of persons are valued in a doctrine of political philosophy, these must ultimately be grounded in states of persons.

If this is problem at all, it is a problem in moral philosophy. In political philosophy, discussants representing positions across the spectrum, including both conservatives and progressives, assume that useful political philosophy discussing the value of fair institutions, of checks and balances, and so on, can be carried out without an argument that these are intrinsically valuable. If an egalitarian wants to argue in favour of retaining the limitation, I contend that the burden is on them to argue its necessity.

Another possible response by an egalitarian pursuing the existing literature is to suggest that they and I engage different philosophical debates and can co-exist. The existing literature pursues a notion of equality as it applies to states of persons and a metric of welfare, while my account pursues questions in broader political philosophy. It might be thought that this amounts to saying that my account engages a different discussion in political philosophy than does that existing egalitarian literature. It might be thought that the existing literature can remain unperturbed in its field of distributive justice, pursuing the relevant set of questions, while my account engages a different set of questions. This would be a misunderstanding. Both sets of questions ultimately address the same political problems, albeit with different emphases. My account pursues a different set of questions only after arguing that the existing egalitarian approach is inadequate to the common political problems addressed, and ought to be broadened to the set of questions I engage. The common political problems addressed are those of understanding egalitarian opinions about the distribution of economic product and justifying these opinions to the conservative opponent. Let me describe the common political problem and contrast my approach to it with that of luck egalitarianism.

4.4 Comparing my account to LE

I describe a conservative position that is perhaps simplistic, and lacking in nuance and detail. This is acceptable as my intention here is not to describe and argue against the views of actual conservatives, but only to contrast my approach to that of LE with respect to the common conservative opponent.

4.4.1 The conservative position

The conservative opponent of the egalitarian may resist progressive attempts at rectifying the individual's poverty, especially in cases where the poverty is not *dire*. The conservative may agree that the poverty is wrong in some sense, but that it only recommends a positive duty not a negative duty. A positive duty is a duty to make the world better by actions with good consequences, while a negative duty is a duty to not make the world worse by actions with bad consequences. It might be accepted that there is a positive duty of charity to help the poor. However, the conservative may think there is no action by non-poor members of society that has the bad consequences of contributing to the poor individual's poverty. Accordingly, the conservative may deny the existence of a negative duty to not worsen the situation of the poor by one's action.

Conceiving of the individual's poverty as a matter of positive duty would suggest an imperative to help the poor individual if one can do so at little cost. The poverty is treated as independent of the non-poor agent and of the government and the situation is akin to that of charity. Viewing the poverty as a matter of negative duty would suggest an imperative for the non-poor and the government to not impose on the poor individual unjust terms for cooperation (such as unfair institutions) that serve to perpetuate or aggravate the poverty. The relevant consequence of seeing the matter in these two different ways is that a conservative who wants to limit government action to the required minimum may think that this minimum includes duties of a negative nature, but not duties of a positive nature. The conservative might say that, as a matter of charity, *individuals* ought to help the poor if they can do so at little cost. If they fail to do so, they are personally culpable. It is no place of the government to, in effect, coerce individuals to help, by taxing them and channelling this to the poor in the form of welfare benefits. The required minimum for the government includes constructing and enforcing necessary institutions of commerce, and ensuring that the operation of the institutions does not harm individuals.

The conservative supposes that something like 'the free market' fits the bill for the requirement imposed on the government. Within this institution, the conservative supposes, all have equal ability to acquire the benefits of economic activity through exercise of voluntary choice and effort. If the government redistributes the economic product generated by a free market, it fails to take adequate cognizance of voluntary choice and responsibility for one's lot. The notion of desert is also relevant, as the exercise of voluntary choice and responsibility within fair institutions is taken to result in the deserved allocation. The conservative holds that taking away some of the deserved holdings of economic product is above the minimum required of a government, and may also be wrong for other reasons.

4.4.2 Luck egalitarian response to the conservative

The luck egalitarian view incorporates the emphasis on choice but notes that an individual's allocation of economic product is not the result *solely* of choice

exercised within an economic institution. It is also partly a result of the influence of brute luck features of the individual. LE holds that desert attaches to the component of voluntary choice, but not to the component of brute luck circumstances. Accordingly, not all of the economic benefits held by the wealthy are deserved, and this provides justification for taxation of some of it. Similarly, the mere exercise of voluntary choice by the poor does not establish that their place in the distribution is deserved. For, their holdings of economic product are affected partly by brute luck factors over which they have no control. The taxed amount can be used to alleviate the poverty that is independently of concern to egalitarians. Such redistribution to the poor does not imply that the egalitarian fails to duly attend to voluntary choice, as choice is not the only determinant of wealth.

It is unclear whether LE casts egalitarian policy as a matter of negative duty. It does not discuss either action to help the poor if one can do so at little cost (as in a positive duty), or action to ensure that the operation of institutions does not harm individuals. LE simply notes that not all of the wealth of the non-poor is deserved and that the level of wealth of the poor is not entirely deserved either (there are brute luck components which are not a matter of desert).

4.4.3 My response to the conservative

In justifying progressive redistribution and related institutional reform, I appeal to reasons relating to political, economic, legal and other social institutions. LE questions the conservative belief that the non-poor deserve their holdings of economic product and so should not be deprived of it. It also questions the belief that government redistribution to the poor always fails to duly emphasise choice. My account can sympathise with this reasoning in luck egalitarianism, but has more to add. It also answers the conservative by noting factors like unfairness which form the background to holdings of economic product. I can agree with the conservative on the value of voluntary choice and responsibility. I differ in calling attention to the objectionable features of the institutions within which choice is exercised.

Note that this relates back to section 3.3.3.2 of the previous chapter where I argued that the common ground of responsibility is not the only way for egalitarians to justify their claims to conservatives. Conservatives share with egalitarians a concern for values like fairness, and for proper institutional design with adequate checks and balances.

My account does not focus merely on states of a person or on the belongings of a person. It focuses also on various social institutions. This is in keeping with the notion of equality implicit in a term such as political equality. In terms of the distributive justice debate, the institutional focus is similar to the way in which the conservative focuses on the institution of the market. When the conservative perceives an injustice in distribution of economic product, this is not because of the state of the wronged person, but rather because of the free market failing to function justly.

My response to the conservative does not require commitment to an egalitarian patterning constraint. This is an advantage over LE, as the conservative can demand justification for the latter's commitment to the patterning constraint. As discussed in chapter 3, no such justification is forthcoming. Since my view does not consider the value of equality in terms of a distribendum to be distributed, there is no commitment to a pattern of distribution.

Some of the instances of objectionable inequality picked out by my account would also be picked out by the LN principle. For instance, consider an objection based on insufficient voice in the design or running of an institution which caused the inequality. The luck egalitarian might say that the inequality was not caused by the worse off person's choice; it was caused by an institution which she did not design or consent to. Thus it is caused by brute luck and is already covered by LE. However, there are important differences in the competing reasons for the objection presented by the two views.

The LE reason requires discussion about where a person's agency ends and where brute luck begins. The competing reason focuses on different and, in a sense, more tangible things. It focuses on the nature of an institution, its provisions for ensuring the views of affected parties are sought, its checks and balances to ensure that the interest of one affected group or the decision-makers themselves do not unfairly and systematically overpower the interests of others. Placing the burden of proof on a scrutiny of institutions, rather than of individuals, can sometimes make it easier for the egalitarian to argue her case. Institutions are generally open to view, and the egalitarian and the conservative are likely to share common ways of assessing them, such as checks and balances, constitutions, and consulting mechanisms.

There are factors other than choice which can serve as common ground with the conservative, and thus feature in a convincing egalitarian case. On a given issue, the egalitarian may find it strategically wiser to focus on the institutional concerns than on the role of luck to convince the conservative. For example, in a case of differences in brute luck natural abilities (such as Scheffler's talented athlete example), it may not be very convincing to argue that this difference is the reason that the resulting inequality in distribution is objectionable. It may be more convincing to argue that the resulting inequality is objectionable because of the social institutions which attach unfair rewards to the possession of various talents (Scheffler 2003: 32-3).

Moreover, note also that, in highlighting objectionable features of institutions, there is a negative duty to rectify the situation and not merely a positive duty. The duty is to ensure that the non-poor and the government do not impose institutions that perpetuate the poverty or marginalization of the poor. Establishing a negative duty (rather than a positive one) to carry out progressive reforms is a powerful tool in effecting progressive change. It is likely to be easier to mobilise people to act if the action is construed as correcting previous actions (such as perpetuating an unfair institution) which are responsible for harm, than if the action is construed as alleviating suffering for which one is not at all responsible. Thomas Pogge has used this distinction forcefully in arguing for a negative duty, rather than a positive one, to enact certain progressive policies of international justice (see chapter 5, section 5.2.2). My account applies the strategy in political philosophy more generally.

This concludes my discussion of the alternative account of equality insofar as it relates to the recent egalitarian distributive justice debate. In the next chapter I explore the alternative account further, but this time in relation to other positions in broader political philosophy. I attempt to give an indication of what would characterise egalitarian philosophy.

Chapter 5: Egalitarianism as a position in political philosophy

In this chapter, I undertake two tasks. The first is to describe my account of egalitarianism in greater detail and the second is to introduce the case study which will occupy the rest of the thesis. Together, these two tasks characterise what I call egalitarian philosophy.

Section 5.1 further describes my account of equality. Whereas in the previous chapter, I describe it in relation to the existing egalitarian literature on distributive justice, in this chapter I relate it to other positions in political philosophy. In section 5.1.1, I consider whether the egalitarian intuitions suggest any particular ideology or ideal to characterise egalitarianism and unite the diverse intuitions under one umbrella. No such theme is apparent. I propose that egalitarianism is problem-based and not ideal-based.

In section 5.1.2, I present similarities between egalitarianism and other positions in political philosophy on certain problems. Section 5.1.3 presents some political opponents against whom egalitarians would argue, and some sorts of issues on which they would argue. In section 5.1.4, I note that the account is a deflationist account of equality and I defend this by reviewing some of the arguments from the past two chapters. In section 5.1.5, I turn to the issue of whether egalitarians are likely to be prone to either an interactional or an institutional analysis of problems. I relate this discussion to LE and circumstances.

Section 5.2 introduces the case study that occupies the remaining chapters. The case study is undertaken as an example of how I propose egalitarian philosophy should proceed, under my account. An example is useful with respect to my account, as it is otherwise difficult to describe what unifies egalitarianism as a position. Given the absence of a unifying ideal, a body of work presenting examples of egalitarian philosophy is necessary to convey an impression of the way egalitarians tackle issues, and the sorts of solutions they propose. Such a body of work can only appear in time if philosophers find attractive the project I describe. For my part, I can provide one such example.

5.1 Comparing my account to positions in political philosophy

5.1.1 Ideology and ideals

One general way in which a political philosophy might proceed when confronted with a problem is to follow an ideology. I do not use the term ideology to imply disparaging connotations of unreasonable dogma. Rather, I use it only to mean a doctrine of belief about what are the fundamental sources of social wrongs and what are the fundamental means of desirable social change. The doctrine may or may not be right.

A liberal ideology would be to suppose that a state with some redistribution of income and some provision of public goods is the basic model and that problems should be confronted in terms of how a state can deal with them. The problem would be assessed as to whether it could usefully fit under the public-good umbrella, or could be addressed by redistribution of income or whether the state is guaranteeing the basic liberties.

A Marxist ideology might consider certain sorts of property to be problematic and examine whether a given problem can be traced to this fundamental structure. In wondering how to effect desired change, it might ignore certain classes of society as possible vehicles of change in preference for other classes.

An anarchist ideology of repudiating organised concentrations of power such as governments might conceive a given problem in terms of whether it relates to an organised body of power. It might seek to effect change by means of bypassing organised bodies of power or by undermining or eroding their power. It is likely to seek changes that can be effected by motivated groups of individuals at a local scale rather than government action.

The egalitarian intuitions I list in section 4.1 do not tend towards any of these ideologies. Nor is any other clear ideology apparent. Some of the problems relate to fairness of institutions and these could be addressed by institutional reform. Nor does it suppose that, for any given problem, it is best addressed through use of, or reform of the state. There may be problems that are better addressed by non-state actors. Prominent non governmental organizations, civil society organizations, corporations and international financial institutions, for example, are non-state agents which may be better placed to handle certain sorts of problems.

It is not clear that institutional reform of institutions unacceptable to egalitarians should follow any specific formula. I would expect that liberals, Marxists and anarchists could all share many of the egalitarian concerns and could propose quite different diagnoses of the problem or proposals for change. Individual philosophers working as egalitarians may have idiosyncratic predilections for particular sorts of solutions to problems, but the egalitarian intuitions themselves do not lean towards any identifiable ideology.

Some political visions can describe an ideal state or utopia. The utopia may be one where a free market will solve all distribution and various coordination problems, and, together with a minimal state which administers the liberal freedoms, will also constitute justice. Or, the ideal might be a gift economy with no state and only small autonomous communities. The utopia may be one of representative government with a constitution, or it may be one of deliberative democracy on all matters of politics and economics. Ideals towards which philosophers of a specific political persuasion strive can form part of a methodology in the sense of allowing a way forward; a way of discussing how a given problem is a deviance from the ideal.

The egalitarian intuitions do not suggest any particular ideal that could usefully encompass them all. Egalitarians would find attractive a society in which oppression was eliminated, and all basic needs were met, and so on. These are goals to work towards, and, in that sense, are ideals. However, meeting basic needs or alleviating oppression merely characterise egalitarian concerns. They do not define a goal the achievement of which would end egalitarian concern. They do not describe any one ideal form of social organisation or utopia. They simply describe desirable features of a society.

With respect to the LN principle in particular, many cases of egalitarian concern are also ones in which a person's situation is crucially affected by circumstances and not merely by her choice. However, recall that it is implausible to hold that *all* cases of inequality in which circumstance plays a significant role are, to that extent, unjust. Moreover, it is not clear that people should *bear the distributive*

consequences of their choices but not those of their circumstances simply because they are *morally responsible* for the former and not the latter. Accordingly, the LN principle characterises egalitarian concern in many cases, but certainly does not define it. There is no reason to think that a society in which the individuals' situations are determined wholly by their choices and not at all by circumstances would be a utopia for my account of egalitarianism.

Instead, my account of equality is *problem-based*. This is to say that I propose egalitarians pick up particular problems and seek the best way of resolving them. Criteria for assessing competing proposals include such things as effectiveness, cost, appropriateness to a particular social context, feasibility, sustainability, comprehensiveness, and so on. A single proposal may be judged differently with respect to a criterion when applied to different instances. For example, the effectiveness of a policy may differ sharply depending on whether the society in which it is applied has certain sorts of infrastructure, whether corruption plays a very large role, whether there is a large black market, whether there is solidarity between different groups in the population, whether the country has a sufficient level of national income, and so on. There is substantial reliance on the findings of social science to guide the construction of a proposal, and on empirical research and journalism to understand the context of a particular problem. For an example of what I mean by 'problem-based', see section 5.2.1 below. There I revisit the issue when describing the way in which the problems I choose for my case study suggest (to a degree) a particular way to proceed.

The feature of steering clear of describing a utopia or an ideal structure for society can be related to the problem-based approach as follows. I begin not with an ideal exemplified in a utopia, but with a specific problem. Proposed solutions are judged social-scientifically and empirically. It is likely that the social scientific basis for a proposal is more secure the more the end point resembles the status quo. For, extrapolation from research about the status quo is probably more reliable for smaller changes than for larger ones. Given that utopias are rather distant from reality, it is difficult to justify a claim that one utopia will be better than another in solving the bulk of the egalitarian concerns. It is hard, for example, to justify the claim that representative governments are better than deliberative democracies or free markets better than government intervention for the bulk of the egalitarian concerns. This is even harder when the claim is for all countries whatsoever, given the obvious differences between them.

On my account, egalitarianism is motivated by the desire to do such things as eliminate various sorts of discrimination, reduce various instances of wealth inequality, improve access of the global poor to basic goods such as adequate nutrition, shelter, healthcare and education, release subject populations from control of an elite, improve access of citizens to policy makers relative to corporations, and much else besides. On my account, these aims matter to egalitarians for various reasons each of which apply to some (but not necessarily all) of the aims listed. Here are some reasons: the basic needs of some might not be met to a sufficient level; the interests might be inadequately prioritised in relation to the interests of others; some might be suffering because of factors quite outside their control; some might be dominated by others in the sense of having no effective influence over the background institutions which significantly affect their lives while another group does have such influence; some important background institutions may be unfair.

It is unnecessary on this account to construct comprehensive systems which describe an ideal organisation for society to follow. Accordingly, at least on the terms set by my account, it is not a failure for a theory if it describes no ideal form of social organisation. This is simply not part of the motivation for my egalitarianism.

Let me note some continuity with some aspects of existing egalitarian literature. In chapter 2, I briefly described progressive proposals by Ackerman, Van Parijs and Roemer. These proposals can be treated simply as attempted solutions of given problems. They need not be conceived as contributing to a greater egalitarian ideal beyond the policy being recommended. The proposals *can* be seen as reducing the effects of brute luck on inequalities in income as well as on opportunity to attain certain sorts of other goods of social life. However, they need not be seen in this way. Even if the choice/circumstance distinction is used in constructing a proposal (as it is in Roemer's case), it is not relevant to how the proposal is to be judged.

Assessing the adequacy of Roemer's proposal or of the other proposals by Ackerman and Van Parijs and comparing them to other egalitarian and progressive proposals is a somewhat empirical matter. The assessment and comparison cannot be fully carried out if we consider only the factors on the more abstract side of the egalitarian literature. A proper assessment would have to consider such issues as whether, for a given social problem, a focus on redistribution of wealth (whether *ex post* or *ex ante*) is appropriate and adequate. Some problems are better tackled by other means. For example, by greater government provision of public goods; by construction of certain sorts of physical, legal or political infrastructure; by media campaigns to spread awareness about particular sorts of discrimination; by designing checks and balances or oversight mechanisms for various institutions; by improving economic growth; by diversifying the economy and so on. Assessing egalitarian proposals would also involve considering whether a proposal is feasible in terms of complexity and in terms of the infrastructure and resources available in an economy, as well as whether it is politically feasible in terms of being able to garner enough support in the foreseeable future. One would have to assess costs not merely in terms of resources, but also in terms of whether some other group's interests are being hurt, or there is a curtailing of the freedom of some, or a dangerous precedent of government action and so on.

Thus, the proposals can be assessed in isolation from any commitments to a broader egalitarian ideal, simply by the effectiveness at solving the relevant problem.

5.1.2 Agreement with elements of existing political traditions

Even though there is no particular ideology to egalitarianism, egalitarians can agree with philosophers of other labels on many points under *ceteris paribus* clauses. For instance, it is preferable to have constitutionally bound legislative and executive powers than to have an autocrat; that it is preferable that various liberal freedoms be protected than not; that it is better that some social safety nets exist at least for those who cannot meet their basic needs; that there be democratic channels whereby all citizens can determine the major economic, political and other social institutions that affect people's lives and that form the background against which they act.

One way to see this common ground of agreement with philosophers of other labels is to suggest that egalitarianism accepts parts of the visions of *the ideal society* propounded by republicans or by liberals or radical democrats. However, I prefer to

cast this common ground with existing philosophical currents in terms of strategies against particular sorts of problems.

One sort of problem is that of autocracy or dictatorship or monarchy, where the lives of the bulk of the population are determined by the whims or interests of a ruler or a small elite. An attractive general way to mitigate this problem seems to include constitutions and checks and balances on various powers. Philip Pettit's 1997 book is a detailed treatment of such proposals under the banner of republicanism.

Another sort of problem is that of inability to voice one's criticisms of a powerful political, religious or other institution. One way to deal with this is to view freedom of expression as a basic freedom to be protected by the state. Liberalism treats this freedom and various others in this way.

Another sort of problem is the lack of a significant voice in determining the design or actions of the major institutions which affect your life chances. The radical democratic suggestion of increasing the channels of democratic control over various institutions – ideally through direct, deliberative democracy – is an attractive project with respect to this problem.

These proposals for mitigating various sorts of problems or oppressions are attractive. However, I see no justification for the claim that the proposals constitute ideals for the organisation of society which can be used to describe a utopia. The more humble claim I support, is that they are solutions to particular problems. Not all problems of concern to egalitarians will be best addressed by these proposals. The proposals will be tangential to the solution of some problems, which may be equally well solved under, say, either democracy or autocracy. Further, pursuit of these proposals is not always advisable given the conflicting urgencies of different problems. For example, it may be inadvisable to pursue the replacement of autocratic rule by a multi-party election system if a country is afflicted by war and famine, and if it seems that these problems would only worsen during the requisite power struggle.

There is, of course, a more general progressive nature to the account of egalitarianism I present. This is a commonality shared generally with republicans, liberals, libertarians, and radical democrats. The progressive stance relates to the value placed on such things as being able to voice one's criticisms of powerful institutions or having the ability to participate in the design of the major institutions that affect your life. It sees certain institutions or states of affairs as problematic and sees certain sorts of change as desirable. These are general progressive values, but fall short of describing a political ideal or utopia.

5.1.3 Who do egalitarians oppose in political debate?

To improve understanding of a position, it can be compared to rival positions. Thus to improve understanding of egalitarianism, consider whom egalitarians oppose. Since the view is not ideal-based or utopia-based, I cannot compare egalitarianism against an ideal proposed by a competing view.

At a more abstract or theoretical level, it is hard to see why someone would oppose egalitarianism as I have described it. The aims of helping needy people or the worst off or the oppressed or those who suffer from bad brute luck are very general, and it is hard to imagine a morally sensitive person who would not accept those aims. After all, the aims are mere characterisations and thus more widely acceptable than specific prescriptions such as a particular pattern of distribution.

We can, however, consider who egalitarians set themselves against *in practice*, rather than at a more theoretical level. One, egalitarians set themselves against people who (in certain cases) do not want to help needy people or the worst off or the oppressed or those who suffer from bad brute luck. These opponents need not voice their views in philosophy or in *public* discourse. They need not be able to morally defend their views. They may acknowledge the moral wrongness of the status quo and may be convinced that a particular egalitarian proposal would alleviate that wrongness. Nonetheless, they may resist the proposal or its implementation because it would impose costs on them. They may simply be reluctant to lose some of their power, wealth, comfort and lifestyle.

Two, on a given issue, egalitarians seek to dispel disinformation and to cut through simplistic arguments and rhetoric (though they are certainly not the only ones who do this). They can do this either to clarify morally pertinent facts or to get to the crux of the issue and propose well-considered policies whose feasibility and effectiveness is supported by empirical considerations. They thus set themselves against political agents and opinion shapers (including media outlets) who peddle such rhetoric, perhaps for their own political, financial or ideological ends, but perhaps also for other reasons.

Countering disinformation and rhetoric may involve defusing simplistic arguments such as that all taxation is theft. (Liberal equality's balance of the values of liberty and equality, and the left-libertarian tradition do this well.) Or it may involve highlighting parts of history that are commonly ignored, such as colonialism, military interventions and unfair treaties. Or it may involve clarifying research in contemporary social science to show the weakness of a simplistic position such as that unfettered free trade is the best means of development for all countries.

The opponents are not necessarily positions in political philosophy. They are, however, real political agents. The case study I present in the second half of the thesis is an example of such egalitarian investigation.

My account of egalitarianism casts a very wide net. It would ascribe the adjective 'egalitarian' to much existing work which may not describe itself as egalitarian or even as having a basis in political philosophy. It would include work in a large range of disciplines encompassing economics, sociology, politics, ecology, cultural studies, mass communications, development studies, geography, social work and others.

Some ideas by prominent writers which I would consider egalitarian include Thomas Pogge's discussion of the resource privilege and the borrowing privilege of authoritarian rulers to reduce the pay-off of coups d'état (Pogge 2001: 20ff; 2002: ch 4,6) and Joseph Stiglitz's idea of reform of the rules of international trade (Stiglitz and Charlton 2005). Note that Pogge is not part of the existing egalitarian literature (characterized in terms of the currency of equality and equality or what debates) and that Stiglitz is not a part of academic political philosophy.

5.1.4 Deflating egalitarianism

It may be clear to the reader by now that what is emerging is a deflationist account of equality. It is deflationist because the described political philosophy does not appear to be a unique perspective distinguishable from political progressivism in general. Egalitarian intuitions are diverse and do not appear to be unified by a substantive definition or ideal of equality. The values invoked by the intuitions are not

restricted to that of equality. Progressives generally share the intuitions and the values. Many of the opinions I call egalitarian may as well be called progressive.

This deflationist feature is not problematic. I take it that egalitarianism is a political philosophy intended to capture what is behind egalitarian intuitions and opinions. Due to the diversity of the intuitions and opinions commonly called egalitarian, and the similarity of these opinions to progressive opinions, the political philosophy that captures these opinions turns out to be deflationist in the relevant sense. Even though it is a deflationist account of equality, I argue that it is preferable to the accounts in the recent egalitarian debate on distributive justice.

Consider two possible ways in which to judge LE as a theory of distributive justice. One way is to judge by the general progressive intuitions about when a distribution of economic product is objectionable. This avenue finds LE inadequate, as I noted in section 3.3. In section 4.2, I showed other ways in which egalitarian intuitions apply to the distribution of economic product that are not captured by LE. Egalitarian intuitions include intuitions about political, social, and legal equality, and not merely about equality as a pattern of distribution. The diverse intuitions are better matched by the deflationist account.

Another possibility for judging LE as a theory of distributive justice is that perhaps equality need not be understood in the sense of intuitions about political, social and legal equality. Perhaps, for the realm of distributive justice, it is to be understood in a distributive sense only: as equality in the distribution of something, such as states of persons. This would suggest that the advocacy of a particular pattern of distribution is what qualifies a view of distributive justice as egalitarian. However, as I argued in section 3.2, the egalitarian patterning constraint cannot be justified.

It might be supposed that my deflationist account is simply not philosophically satisfying and that philosophers should persist with the recent egalitarian tendency to conceive equality in a distributive sense in approaching distributive justice: even if a justification for the patterning constraint is not available now, it may be in the future. However, I see no reason that such a distributive account should be thought philosophically interesting in itself. An egalitarian perspective on distributive justice may well flow from a wider sense of respect for the value of political equality (even if a formalised understanding of such a value is unavailable.) However, if the egalitarian perspective on distributive justice is not thought to relate to the value of political equality, but is simply a veneration of distributive equality in isolation, then opponents of egalitarianism rightly ask why one should care about this particular pattern of distribution.

LE has moved away from advocating any particular pattern of distribution to advocating equality of *access to* a pattern of distribution. A potential fetishism of the distributive pattern of equality is avoided by the intervention of the criterion of voluntary choice. However, the question remains as to why one should stop at incorporating the value of choice. Surely other progressive values of fairness, democracy, and non-domination can also be incorporated. LE suggests that it is unjust if differences in holdings of advantages arise from factors other than choice. One could likewise claim that such differences are unacceptable if they arise from unfair institutions, or from lack of democracy in the design and running of the major institutions that determine the distribution of economic product, or from the interests of some being improperly dominated by others.

LE is a form of progressive philosophy. What makes it a *distinct* subset of progressive views is that it defines egalitarianism as involving the combination of the values of choice and distributive equality *and nothing else*. Thus, other progressive opinions are excluded. My account is deflationist because it fails to distinguish cases of egalitarian opinion from other cases of progressive opinion. However, as I explained in the previous paragraph, there is no reason why egalitarianism should incorporate the value of choice but not other values commonly defended in progressive opinion, such as fairness, democracy and non-domination.

Consider two possible objections to a deflationist account of equality. One possible objection is the charge that such an account is philosophically useless. This charge is false. The account is not only useful, but, I argue, *more* useful than LE in responding to conservative arguments on issues of distribution of economic product. As I argued in section 4.4, my account shares with the conservative not only the common ground of the value of choice, but also such values as fairness, democracy, and non-domination. It voices progressive objections to the distribution of economic product (in addition to objections regarding issues such as the design of institutions) that relate to these concerns shared with the conservative. The dispute with the conservative lies in demonstrating that particular institutions are unfair, or insufficiently democratic, or lead to domination of the interest of some by others.

Moreover, LE does not play a significant role in identifying wrongs that concern the egalitarian and is unnecessary in guiding practical political reasoning (section 3.3.3). By contrast, the diversity of values and intuitions listed in section 4.1 can identify a wide range of wrongs that concern egalitarians. The values of fairness of institutions, democracy and non-domination suggest many avenues to pursue in political reasoning. The case study in the coming chapters uses these notions of fairness, non-domination and democracy and serves as an example of the utility of this account.

Another possible reason to reject a deflationist account of equality is somewhat aesthetic. Some philosophers may have a preference for an account of a value that is univocal, definitive, and that sets the value apart from related values. I argue that insofar as so-called egalitarian intuitions and opinions exemplify the value of equality, no available univocal and definitive account of equality is fitting, and therefore the only available fit is a deflationist account. I argue that not only is the deflationist account philosophically useful, it is even more so than the LE account. A search for a univocal and definitive account of a concept is often (but not always) helpful. It can force philosophers to clarify ideas and can lead to new insights about how to solve problems. In this case however, the alternative account seems perfectly adequate and a univocal, definitive account does not appear necessary.

5.1.5 Interactional and institutional moral analysis

Thomas Pogge distinguishes *interactional* from *institutional* moral analysis. Interactional moral analysis deals with actions and consequences of actions performed by agents and collective agents. Collective agents include, for instance, a corporation or a government department. Institutional moral analysis investigates effects of the way our social world is structured by rules, practices and social institutions. Such institutions define and regulate property, the division of labour, sexual and kinship relations, political and economic control. They govern how collective projects are undertaken and executed, how conflicts are settled and how social institutions themselves are created or revised (Pogge 1995: 241-2).

My approach to egalitarianism leaves open the focus on either interactional or institutional factors. An example of interactional analysis would be a focus on the policies and actions of a particular collective agent such as a belligerent nation. A contemporary example is US government action in initiating the ongoing war on Iraq in an investigation of various sorts of oppressions in Iraq. An example of institutional analysis would be to focus on the global reserve system and on the system for managing international balance of payments in an investigation of third world debt and of obstacles to development.

Agents and collective agents act against the background of institutions. The belligerence of the US government, for example, occurs against the background of institutions such as the UN. Institutions *within* the US may also be relevant to the investigation. The US mass media or the institution of political funding of presidential campaigns might be thought relevant as enabling factors of the belligerent action. Institutional analysis of these institutions may be helpful, to a greater or lesser extent, in an investigation of oppressions in Iraq.

There may be no clear answer whether a given problem is better discussed in terms of interactional or institutional analysis. At other times, the investigator's familiarity with politics, with the details of the issue and with relevant social science might suggest one sort of analysis rather than the other as more promising.

As an example, consider the problem of global poverty. An interactional approach might propose greater foreign aid to affected populations. This is interactional in the sense that one agent or collective agent (a rich country government) gives voluntarily to another agent or collective agent (a poor country government). This contrasts with an institutional approach, which might look at background institutions such as the global reserve system or the rules governing international trade.

I venture that the option of foreign aid might bring more immediate relief to the global poor, but also comes with no institution establishing or enforcing long term commitment to such aid. The institutional proposals do have this advantage. However, they are perhaps likely to be less predictable in their effects on various groups of global poor. Benefits are likely to appear in the longer term and will be contingent on implementation of adequate domestic policies to take advantage of changes in the global institutions. They will accrue unevenly for reasons of the geography, size and resource endowments of countries. In this case, it seems the interactional and institutional proposals have different costs and benefits, and would ideally be complementarily implemented rather than treated as substitutes.

5.1.5.1 Institutions and circumstances

Given the prominent place of the choice/circumstance distinction in the existing egalitarian literature, let me briefly explore how institutional analysis relates to that distinction. Consider some examples of institutions that form the context for people's voluntary choices, such as political, economic and social institutions.

The *social institution* of caste hierarchy may condition voluntary choice when, for instance, a lower caste individual chooses not to take up an opportunity for tertiary education because she thinks she will be subject to humiliation, harassment and abuse from upper caste classmates. Or again, a social institution of intolerance towards diversity in sexuality may condition an individual's choice to enter into a lifelong relationship in which she expects to find no lasting happiness. *Economic institutions*

can condition voluntary choice when, for instance, an agent chooses to work in a dangerous chemical processing plant without adequate safety measures because adequate government safety regulations are absent and high unemployment and a poor safety net make it imperative to accept available jobs. *Political institutions* can condition choice when, for example, someone chooses to suffer under the self serving rule of local elites because there is no effective political means to contest the power of that elite. *Bureaucratic institutions* can condition voluntary choice when, for example, an individual chooses to spend money desperately needed for medicine to instead bribe a bureaucrat to get a desperately needed ‘free’ food ration card because there are no ways of getting around the corruption.

In some cases, one might say that these institutions condition choice without directly contributing to an individual’s distributive allocation of relevant goods. They could well have chosen otherwise despite the institutions, but the institution changed their perception of costs and benefits and of the avenues open to them. In other cases, one might say that the institutions are among the circumstances directly contributing to the individual’s place in the distribution.

Conceiving of certain factors as *institutions* that condition choice rather than merely as *circumstances* that condition choice has certain consequences. Conceiving a factor simply as a circumstance leaves it open how it should be dealt with. One may simply mitigate its effect by redistributing income ex post in favour of an individual who is disadvantaged by it. By contrast, to focus on the factor *as an institution*, suggests it should be dealt with as such. It is natural to change the institution in order to remove the tendency to produce those particular disadvantages in that particular way. This is not to say that conceiving of factors merely as *circumstances* that condition choice rather than as *institutions* that condition choice is bound to be merely ex post redistributive. Rather, the institutional focus simply places greater emphasis on institutions and makes their role more explicit, even at the stage of diagnosing the problem.

In addition, an institution may be objectionable for various reasons other than its distributive effects. It may have been discriminatory or unfair (say, privileging those whose ancestors were large landowners), or may have unnecessarily restricted the proportion of people in an economy who can earn a living wage. It is one thing to change an objectionable institution and another to compensate people for its effects while it remains unchanged. An institutional focus makes these other objectionable factors explicit.

The choice/circumstance distinction matters to luck egalitarians because humans are responsible for choices, but are not responsible for their circumstances. There are intuitive reasons in favour of making people bear the consequences of factors for which they are responsible. There is no similar reason why people should bear the consequences of factors for which they bear no responsibility.

In earlier chapters I criticised the luck egalitarian explanation for why certain wrongs in society matter to egalitarians. While it is adequate in many cases for the luck egalitarian to express a social wrong in terms of how it requires an individual to bear the cost of some factors which are matters of brute luck, this explanation seems inadequate in other cases. As an example of such a latter case, I presented in section 3.3.1 the example of Scheffler’s naturally talented athlete. It turns out that focusing on institutions can yield a more satisfactory explanation of why certain wrongs and not others matter to egalitarians.

Scheffler suggests that the philosophically and politically relevant sort of unfairness does not lie in natural differences such as those between the talented and less talented athletes. Rather, unfairness attaches to the social context within which natural differences are found. It is not the fact that people are born with different degrees of talent and ability that we find unfair, but rather the fact that we live in a society in which those with some class of talents are given great material rewards and elevated social status whereas those with little talent or with talents in areas that the market and society in general do not value very highly, often find themselves with a relatively meagre lot in the distribution of advantages. Unfairness may attach to inequalities that result from the social context and social institutions. However, the *reason* these inequalities are unfair is not because the social context and social institutions are circumstances beyond the control of individuals. Rather, it is because the social context and social institutions are themselves unfair (Scheffler 2003: 32-3).

5.2 Introducing the case study

Even though my account of egalitarianism is deflationist, it can be thought to name a particular tendency in political philosophy. In the absence of a unifying ideal (section 5.1.1), and faced with a diversity of egalitarian intuitions, it may be difficult to see what characterizes egalitarianism as a tendency in political philosophy. The way forward is to note the ability to identify progressive views in the absence of a univocal and definitive account of ‘progressive’ by instead drawing on awareness of the body of work carried out under the label. Similarly, I claim that what characterizes egalitarianism will be a growing body of work of egalitarian explorations of problems. This will give an indication of the sorts of problems that concern egalitarians and the types of solutions they tend to propose. I have given some indication of egalitarian concerns and egalitarian solutions by noting similarities between egalitarianism and other positions, and by noting some of the issues on which egalitarians would oppose others (sections 5.1.2 and 5.1.3). I have also noted some examples of writers and works that could be described as egalitarian. However, perhaps the best way forward is to simply explore some problems from an egalitarian point of view to yield an example of egalitarianism in practice. As an example of how I propose egalitarian philosophy should proceed, I consider a particular nexus of issues of concern to egalitarians and investigate it with the aim of reaching some proposals for egalitarian change. This case study occupies the remaining chapters of the thesis.

There are many issues competing for the egalitarian philosopher’s attention. Let me say a little about my choice of issues for the case study. Elizabeth Anderson has noted that the concerns of some recent egalitarian writing invite a perception that egalitarianism has relatively frivolous motives. Ronald Dworkin (Dworkin 1981b: 285) relates equality to an ‘envy-free’ distribution of resources, inviting the perception that egalitarians are motivated by mere envy. Philippe Van Parijs (Parijs 1991) argues that the values of equality and liberal neutrality require the state to support lazy, able-bodied surfers who are unwilling to work, inviting the perception that egalitarians support parasitism on the toil of others (Anderson 1999: 287). A ‘hard case’ such as the surfer example has the advantage that it might sharpen our understanding of what motivates egalitarians simply because it stretches our intuitions beyond the cases where we have ready answers. In the absence of a ready answer, we must reason about what motivates egalitarian concern or what egalitarians aim to do.

Egalitarian intuitions are diverse and no substantive theme or ideal is apparent to unite them. I expect that there are *many* reasons why the sorts of cases that concern egalitarians matter to us. Accordingly, while considering hard cases like the surfer example *might* clarify certain motivations animating egalitarians, there is also something to be said for considering the problems which matter to egalitarians *most urgently*. This too clarifies certain motivations. It might even clarify motivations that most *commonly* motivate egalitarians and perhaps ones which are more *central* to egalitarianism than the ones that emerge when we consider a hard case such as the surfer example. Judging by the most urgent claims of concern to egalitarians, egalitarians are motivated by such aims as eliminating oppression, injustice, servitude, domination, exploitation, dire poverty.

Moreover, recall that I expect egalitarianism to proceed problem by problem. In a choice of problems to investigate in the hope of resolving them, there is surely a (defeasible) moral imperative for egalitarian philosophers (qua moral agents) to consider more urgent wrongs and suffering rather than comparatively minor ones. Among the more urgent such issues are those regarding the under-development of poor countries and the absolute poverty of their poorer citizens.

5.2.1 WTO, international debt and the global reserve system in relation to development and global poverty

I take it as given that global poverty is a grave problem and so I do not build a case for this. I do, however, list a few indicative figures taken from (Pogge 2001: 7-8). About 1.5 billion people (about a $\frac{1}{4}$ of world population) are below the international poverty line. This poverty line is described as “income or expenditure level below which a minimum, nutritionally adequate diet plus essential non-food requirements are not affordable” (UNDP 1996: 222). Around 790 million people are inadequately nourished, 1 billion are without safe water, 2.4 billion without basic sanitation and there are around 1 billion illiterate *adults* (UNDP 2000: 30). About 880 million have no access to basic health care (UNDP 1999: 22). Around 1 billion are without adequate shelter and 2 billion are without electricity (UNDP 1998: 49).

Let me also give some indication of the extent of global inequality. The high-income countries (32 countries plus Hong Kong), with 14.9% of world population have about 79.7% of aggregate global income. For the bottom quintile (the bottom fifth of world population as ranked by annual income), aggregate annual income is one third of a percent of aggregate annual global income. Annual per capita income in the high income countries is \$27,510, compared to an annual per capita income of \$85 in the bottom quintile. Wealth statistics would be even less equal. Affluent people generally have more assets in addition to their annual income and the poor typically own significantly less than one annual income. The income gap between the richest and poorest quintiles of world population has been growing. It was 30:1 in 1960, 60:1 in 1990, 74:1 in 1997 (Pogge 2002: 99-100).

Some social movements charge that institutions regulating international trade and finance contribute to this situation; that the situation mostly benefits the developed countries; and that action by the developed countries, or changes to some international organizations dominated by developed countries, could make it easier for the developing countries to develop and to address poverty.

These allegations are serious. Egalitarians concerned about global poverty seek institutions and agents that either contribute to the poverty, or seem likely

avenues of alleviating some of the poverty. They also seek agents who may have some degree of responsibility for contributing to the poverty, perhaps by implementing or maintaining offensive institutions. The allegations are interesting to the egalitarian because they identify some institutions that are claimed to contribute significantly to global poverty, and to be vehicles by which the poverty could potentially be alleviated. Insofar as the institutions identified are maintained by certain agents (including collective agents such as governments), the allegations also suggest a negative duty on the part of these agents to implement progressive change. For egalitarian philosophers who are citizens in some of the developed countries, this last point may be particularly salient, as they may bear some degree of the negative duty as well, insofar as their governments formally represent them.

These considerations warrant egalitarian investigation of the allegations. I contribute to such an investigation by carrying out the case study. Nonetheless, the case study is not a full egalitarian investigation, and I clarify below the sense in which it is incomplete. The case study presented here merely aims to give an indication of the sorts of issues egalitarians would find problematic, and the sorts of proposals they could find relevant and attractive in solving problems. The case study is included in order to allow a comparison with LE. LE might approach the issue of global poverty and development as a matter of distinguishing factors of circumstance from those of voluntary choice among the factors that contribute to an agent's holdings of advantages¹⁴.

In the case study, I pick out specific institutions on which to focus: the rules for international trade, the institutions of sovereign debt management, and the global reserve system (relating to the way that countries acquire monetary reserves, the reasons they acquire them, and so on). The World Trade Organization is considered in detail as the most important body mediating the rules of international trade. The International Monetary Fund and the World Bank are discussed in relation to their roles as lenders and as mediators with respect to sovereign debt. The International Monetary Fund is also discussed in relation to its role in the global reserve system.

There are many contributing factors to global poverty. My choice of focusing on these factors rather than on others is due simply to my preoccupations and general political awareness. Such idiosyncratic facts about the individual philosopher affect the sorts of problems thought relevant, and the sorts of contributing factors thought likely to be most illuminating in an investigation of a problem (see section 3.3.3 in chapter 3 for a discussion of preoccupations in relation to LE).

On my account, an egalitarian approach to issues of global justice, global poverty and development is not committed to any particular way of conceiving the debate. It is not committed to emphasizing the individual nation-state as the prime agent for change and the focus of investigation, asking what policies a national government should follow to improve its economic performance. It is not committed to the view that the prime focus of the investigation should be inter-*national* politics. It allows the possibility that *non-state* actors such as corporations, NGOs, civil society groups, paramilitaries, international treaties and organisations such as the IMF, WTO

¹⁴ In this connection, see Cappelen 2005 for an investigation of how the luck egalitarian approach, based around the choice/circumstance distinction, might apply globally. Taking the primary agents to be nations (rather than individuals), he finds that new problems in applying the LN principle crop up at the global level which do not at the domestic level.

and development banks play significant roles both in the problems and in their solutions.

The nature of the problem naturally suggests engaging with certain academic disciplines outside of traditional political philosophy. For instance, the issues cannot be adequately addressed without engaging with the economics and political economics of international trade and of national debt, as well as the politics of decision-making in the institutions named. Note how this differs from the bounds of the egalitarian distributive justice debate. The parsing of political concerns in that debate seems based on states of persons. Aspects of political concerns that are relevant to states of persons are within the bounds of the debate, and other aspects may be ignored. In the approach I propose, the parsing is not based on the states-of-persons limitation, or on any other presumption about the aspects of a political concern which are most salient for egalitarians. In my approach, the parsing is that the political concern should be considered in terms of the mechanisms that might cause it, and mechanisms that might alleviate it, across any academic disciplines that are relevant to an understanding of the mechanisms. In this sense, the parsing is suggested by the political concern or problem itself. This relates to comments in section 5.1.1 that describe my view as problem-based.

The case study mostly looks at *institutions* that influence global poverty (although the chapter on sovereign debt also focuses on *particular lenders* rather than merely on institutions). To relate to section 5.1.5, the case study is mostly an example of institutional moral analysis.

While the case study is multi-disciplinary, it remains also a piece of political philosophy partly because of some normative conclusions. The normative component to this investigation would be the prescriptions for change that seem most desirable as a result of the investigation. The case study remains political philosophy partly also because there is no other way to understand philosophically the value of political equality, than by building a body of egalitarian investigations of problems (or so my account of equality would have it)¹⁵.

Nonetheless, the case study is not a full investigation of the relevant issues. I undertake the case study as an example of egalitarianism in practice. I do this partly in order to better present my account of egalitarianism and partly for the sake of investigating some issues of global poverty. A full exploration of the relevant issues would have to be more extensive in some ways. It would have to consider for example, other proposals for reform to the same institutions. I do not consider all proposals or all approaches to the institutions. A full investigation would compare the proposals I present in coming chapters, against competing proposals and would assess the likely costs and benefits of each, the political likelihood of each being implemented, and so on. It would also consider other factors (than the three institutions of trade, debt, and reserves) that contribute to global poverty and assess which institutions are most amenable to constructive change.

However, I need not undertake a full investigation in order to contrast my approach to egalitarianism to that of LE. The case study provides examples of the way that I envision egalitarians approaching problems, of the sorts of institutions that

¹⁵ My description of liberal, republican and radical democratic ‘ideals’ as proposed answers to particular problems (section 5.1.2) perhaps suggests that this is also true for philosophical understanding of positions other than egalitarianism.

might be thought worthy of discussion, of the sorts of proposals that seem attractive, and of the sorts of reasons why egalitarians find proposals attractive. These are all ways of contrasting the account with LE. In discussing proposals for change, I choose proposals that are illustrative of the scope and power of institutional reforms in their relevant fields. I advocate the proposed reforms in the sense that I argue them to be promising means to achieving egalitarian goals. I do not advocate them in the sense of favouring them over all other plausible contending reforms in the relevant fields. Advocating the reforms in the latter sense would require a fuller investigation of the issues, which I do not undertake in this thesis. The fuller investigation would expand in the ways detailed in the previous paragraph. Let me now note some contrasts between LE and my approach.

Given that LE is a theory of distributive justice only, it is unclear what the theory would have to say on the rules governing international trade. It may treat these rules as just one among many other factors that are circumstances, rather than choices, in relation to any individual poor person. Or it might treat them as circumstances rather than choices in relation to most of the countries bound by the rules, given the unfair bargaining power in the negotiation process that resulted in the rules. Contrast my approach. It is not limited to states of persons, and so considers such factors as fairness of institutions – in this case, the fairness of the rules of international trade. It considers the institutions not merely as circumstances, but in their own right. The remedy suggests itself naturally for unfair institutions: reform the institutions to make them fairer. This relates to section 5.1.5 above.

For the institutions surrounding sovereign debt, LE might consider such issues as which factors affecting a country's situation it should be held responsible for, and which not¹⁶. My account instead considers such things as whether the institutions are fair in balancing the interests of borrowers and lenders, and whether they are fair in holding a country responsible for debts incurred by an undemocratic ruler.

With respect to the global reserve system, it is unclear what LE would say. Since they are among the determinants of individuals' holdings of advantages, the theory might simply place the system under the 'circumstances' column rather than the choice column. As discussed in section 5.1.5, LE does not focus on institutions in particular nor suggest remedial change to institutions if these are seen to be at fault.

Here is a brief outline of the content of the case study. I begin with an overview of pertinent areas of development economics. I present some basics of economic growth and international trade as it relates to economic growth. I present common arguments in development economics for government action in promoting development and economic growth.

Second, I consider the World Trade Organisation (WTO) and the rules for international trade. I describe the relevance of these rules for the aim of development of the developing countries. I describe the WTO and several of its pertinent rules, focusing on rules for preferential treatment of poor countries. I outline various criticisms in the extant literature of the existing rules for special and differential treatment of poor countries. The system imposes substantial costs on poor countries

¹⁶ See for example Cappelen, Hagen and Tungodden 2008. It is a luck egalitarian investigation of sovereign debt relief.

and fails to adequately prioritise the interests of the global poor (it in fact does the opposite, acting to favour residents of larger and developed countries over those of residents of the poor countries). Progressive reform of the system has the potential to help poor countries develop and to thus help their poorer residents. I advance such a proposal for reform as desirable from the egalitarian perspective. The proposal closely follows ideas advanced by Joseph Stiglitz and Andrew Charlton.

Next, I consider the institutions surrounding sovereign debt. I describe the basic mechanisms of a credit market and present some historical factors behind the crippling debt burden of many developing countries. I describe some of the existing debt relief programs and discuss criticisms of them. I end by considering the issue of sovereign debt from an egalitarian perspective. I propose various changes, some of which make use of ideas by Kunibert Raffer and Thomas Pogge.

Finally, I consider the global reserve system. I describe national reserves and the reasons why governments seek them. I outline the existing global system of reserves and its costs for various countries, both rich and poor. I argue that the costs to poor and developing countries are sufficiently great to motivate the implementation of an alternative that seems likely to impose far fewer costs. I end by proposing such an alternative as desirable from an egalitarian perspective. The proposal follows ideas advanced by Joseph Stiglitz and Bruce Greenwald.

5.2.2 Situating the case study within existing literature on global justice

Let me situate the case study within the context of some existing work in the global justice literature. Here are two debates in the literature. One, relating to international *distributive* justice in particular, is whether egalitarian theories of distributive justice that seem more or less correct for domestic justice (say Rawls' Difference Principle or LN) should be expanded to apply to the whole world. Some, including Rawls, have argued against this expansion. Some of the global justice literature is devoted to considering the relevant ways in which domestic and global justice differ and whether the differences warrant the differential standards for distributive justice domestically and globally.

Van Parijs 2007 is an overview of many such differences. The article concludes that there are strong grounds for expanding the egalitarian theories of domestic distributive justice to the world.

Two, one might consider what sort of duty governments of rich countries, or citizens of rich countries more generally, have to alleviate global poverty. One possibility is that it is a positive duty, while Pogge argues that it is a negative duty. A positive duty is to protect others from great harms and risks if one can do so at little cost. The wrongs are treated as independent of the duty-bound agent and the latter's duty to alleviate the wrongs is akin to charity. A negative duty in this case is to ensure that we do not impose unjust terms for international cooperation on other countries which serve to perpetuate or aggravate the relative and absolute poverty of the global poor. This is, in some sense, stronger than a duty of charity, as it *implicates* the duty-bound in the wrongs that they are to alleviate. Pogge describes some ways in which we in the rich countries (which are also the most powerful countries globally) are *responsible for* the perpetuation of global poverty (Pogge 2001, 2002 (for instance, the introduction), 2005). He speaks of a 'global economic order' which forms part of the background against which countries and other collective agents deal with one

another globally. He suggests that the governments of the rich countries serve to perpetuate this order and that the order contributes to global poverty.

I now situate the coming case study with respect to these literatures. I am not concerned with *distributive* justice in particular. Nor do I begin with an egalitarian ideal at the domestic level which may or may not be applicable to the global level. Accordingly, I do not participate in the debate on whether principles for *international* distributive justice can be read off egalitarian theories of *domestic* distributive justice.

Turning to the issue of responsibility, note that there are various reasons for determining responsibility for the situation of the global poor. One is as a matter of theoretical completeness for a philosopher discussing these wrongs. Another reason is that the issue has practical value as a tactic for change. Let me explain.

I identify global poverty as a problem of concern to egalitarians. I narrow my concern to one factor relevant to global poverty, namely 'development'. I narrow further in considering a couple of global institutions relevant to development namely the global reserve system and the WTO. I argue that these institutions have some effect on the possibilities of development of poor countries and on the amount of national income they can spend on poverty alleviation. I argue that the institutions serve to perpetuate or aggravate the under-development of the poor countries and their ability to increase national income or spend an adequate portion of that on domestic poverty alleviation. I argue that, worse still, aspects of these institutions are *to the benefit* of sections of the rich developed countries *at the cost* of the poor countries.

These institutions concern egalitarians because they are among the factors that perpetuate global poverty and because they are arguably unfair and unjust. Promising proposals are available of how to improve matters (including, I contend, the ones I discuss in coming chapters) and they seem not to have prohibitively high costs. The proposals should, therefore, be serious candidates for implementation.

Consider the group of people who may be motivated to try and enact such proposals. The group will include agents who stand to gain materially from the change or representatives of such people. This includes civil society groups, business groups and governments of poor countries. The group will also include those who are morally alarmed by the injustice, which includes many groups in the rich countries (whom we would include among egalitarians) who do not foresee any material gains *for themselves* from the progressive change.

Egalitarians can explain why they want to effect these changes and seek popular support for them in many ways. They can point out that the existing institutions are *unfair* – benefiting some (sections of rich country populations) at the expense of others (the global poor). They can explain that the design of the institutions fails to adequately *prioritise* the interests of the worse off and, in many ways, prioritises the interests of the better off. They can emphasise that the institutions contribute to abject poverty in terms of inability to meet any reasonable threshold of the satisfiers of basic needs. Many hundreds of millions are below or perilously close to any threshold of *sufficiency* of the satisfiers of basic needs that can reasonably be drawn. Improvements in the institutions (together with appropriate complementary policies) could reasonably be expected to aid poverty alleviation for the abject poor.

All of these are reasons that can motivate citizens and governments of the rich countries to act to alleviate global poverty. However, arguments to convince rich

country governments and especially the corresponding voting publics that they are *responsible* for global poverty are especially powerful motivators that can hasten remedial action by them. Rich country governments are in a very strong position to contribute to poverty alleviation. Given that egalitarians want to take steps to alleviate global poverty, establishing culpability of rich governments in this poverty is a powerful political tool in effecting that change.

Linking back to Pogge and the discussion of responsibility for global poverty, rich country governments' responsibility for various instances of oppression of developing country peoples and for many aspects and instances of global poverty, can be easily established¹⁷. The institutions I consider in the case study are part of the 'global economic order' discussed by Pogge in relation to establishing responsibility of rich country governments for global poverty. Moreover, making the arguments about responsibility widely known to developed country citizens is likely a necessary (but by no means sufficient) means of effecting progressive change.

Nonetheless, I do not undertake the task of determining responsibility of rich country governments and elites for the problematic design of the institutions I discuss¹⁸. I am concerned only to establish that certain institutions contribute to global poverty and to under-development of many countries and to propose alternatives that could accomplish the necessary functions of the institutions while not harming the poor countries in the ways discussed and while helping them in some ways.

¹⁷ For just a few examples, see Pogge's work on the borrowing privilege and the resource privilege (Pogge 2002: ch 4, 6); or (Monbiot 2003: ch 4) on the unequal distribution of power in the United Nations; or (Chomsky and Herman 1979) and (Blum 2002) on some of the covert and overt military interventions by the US government to maintain or bring to power rulers in various poor countries who sometimes tyrannise their domestic populations and generally perpetuate a division of national wealth grossly to the benefit of small elites and fail to address domestic poverty.

¹⁸ To establish responsibility, relevant factors include the greater bargaining power and influence of the powerful few countries (and especially the US) in the design of the Bretton Woods (BW) institutions and existing biases in policy and decision-making. Here are some places to begin the investigation. Peet 2003 treats the BW institutions individually from their inception, through changes in policy direction, to the time of writing. Stiglitz 2002 discusses the performance of the World Bank and IMF, in the East Asian economic crisis of the late 1990s and the treatment of Russia in the 1990s. To make sense of the otherwise puzzling IMF policy over that time, Stiglitz suggests that we view IMF policy as strongly determined by the interests of the financial community (especially in the US, but also in a handful of other powerful economies), to the detriment of the poor of borrowing countries (Stiglitz 2002: 206ff). For the responsibility of developed country governments and the international financial institutions in encouraging over-lending by developed country banks and the contribution of this to unsustainable external debts in many developing countries, see Raffer and Singer 2001, particularly ch. 10, 11.

Chapter 6: The economics of development

This chapter presents some background economic theory on the issues of economic growth, international trade and development. Familiarity with these issues is requisite for the discussions in coming chapters.

Let me set this chapter's discussion in the context of egalitarianism. The egalitarian concern motivating this case study seeks ways to alleviate global poverty. International trade can affect a country's economic and infrastructural development, and national income. This in turn can affect how the global poor fare. Let me note a few ways in which the poor may be affected.

Greater national income allows the government of a developing country more wealth with which to alleviate poverty. A flourishing export industry can generate employment both directly, and through flow-on effects in complementary sectors of the economy. Access to cheaper and better quality goods from imports can improve standards of living. This applies not only for manufactured goods, but also for food grains and other essentials.

The infrastructural development which is likely to accompany economic development may have positive effects for the standard of living of the global poor. There may be improvements in infrastructure such as road, rail, and telecommunications, or in institutions such as laws, educational and training institutions, or in bureaucratic and administrative processes, and so on. More, and better, roads allow easier freedom of movement and migration, as well as access to essential resources. Improved communication infrastructure can allow improvements in news media coverage of previously marginalised groups. Import of technology and know-how can help in many ways, depending on the relevant sector of the economy.

There are also distributional effects of international trade. There are gainers and losers within each country and also broader distributional effects between trading countries. A government can use interventionist trade policy to change the distribution of gains and losses both within a country and across countries. To emphasise the relevance of international trade to international distribution of wealth, consider the size of annual official development assistance (or ODA) in relation to the effects of trade on developing countries. ODA is the assistance administered by the members of the OECD, via its Development Assistance Committee. In the absence of trade restrictions by the developed countries, developing countries could realise an additional \$700 billion annually in export revenue. This is a large amount of money for the developing countries – roughly 11% of the aggregate annual gross national income of all developing countries. It is also 12.5 times the annual ODA (Pogge 2002: 18).

Government intervention can also shape the growth of an economy in a certain direction. For example, it could promote one industry rather than another. In the next chapter, chapter 7, I consider the World Trade Organization (WTO). As a general description (for some important qualifications and exceptions, see the next chapter), the WTO seeks to get its members to reduce to zero any interventionist trade policy such as tariffs or subsidies. This affects the options available to governments to pursue different distributions of gains and losses, both within a country and internationally, and affects the ability to shape an economy's growth in a particular direction. These are reasons for examining the WTO in the context of an egalitarian investigation of development. In turn, that examination necessitates an overview of

the economic rationales for interventionist policy and the ways in which such policy can affect distributions of gains and losses. I undertake this task here.

In section 6.1, I present the foundational arguments that under perfect competition and in the absence of market failures, free international trade can be good for all trading countries. I present the theory of comparative advantage and the Heckscher-Ohlin model.

In section 6.2, I consider some common market failures specific to the issue of development that provide rationales for government intervention. In particular, I consider coordination failure, increasing returns to scale, learning-by-doing, and dynamic comparative advantage. In section 6.3, I describe some instruments of government intervention in international trade.

In section 6.4, I present some expected gains and losses from trade between different types of countries. This relates to the point that international trade can be a vehicle of redistribution of wealth both within a country and across countries. This sets a context for chapter 7, where I focus on international trade as a means of international wealth redistribution.

6.1 The possible benefits of trade

6.1.1 The theory of comparative advantage

The theory of comparative advantage holds that when two countries X and Y trade in two goods G and H, both can benefit by specialising in the good in which they have comparative advantage and then trading the goods. Country X may have an absolute advantage in both goods. That is, it may be more efficient than country Y in producing both goods. Nonetheless, country Y will have a comparative advantage at producing one of the goods. The scarce resources which are used in the production of both G and H will be more productively employed in the production of one than in the production of the other. When country X commits its scarce resources to producing good G, there is an opportunity cost of not committing them to producing H. Country Y will have a comparative advantage in producing the good whose production incurs the larger opportunity cost for country X.

To consider a simple example, begin with a situation of no trade and suppose there is a single input of production. Suppose it takes country X 10 and 15 units of input to produce a unit of G and of H respectively. Suppose it takes country Y 40 and 20 units respectively. Country X has an *absolute* advantage in both goods. However, consider the *relative* input cost of the goods. In X, a unit of G costs $\frac{2}{3}$ of an H ($\frac{10}{15}$). In Y, a unit of G costs 2 units of H ($\frac{40}{20}$). Even though X has lower *absolute* prices for both goods than does country Y, the latter has a lower *relative* price of H. It thus has a comparative advantage in producing H. In this model, each country will always have a comparative advantage in one and only one of the goods except in the case where the two countries have the same relative price in a situation of no trade.

Country X has a lower absolute cost for producing both goods. Yet, if it specialises in G and imports H, the units of input freed up from abandoning production of H will produce more units of G than they produced of H. Likewise in Y. If it specialises in H and imports G, the units of input freed up from abandoning production of G will produce more units of H than they produced of G. With specialisation in one's area of comparative advantage, the combined production by

both countries of each good G and H rises when compared to the combined production of each in a situation of no specialisation. If the countries trade, as well as specialising, they can share the benefits of this greater pool of goods.

Countries can have a comparative advantage for reasons such as differences in technology or in endowments of factors of production such as arable land, human capacity, and skilled workers.

6.1.2 Heckscher-Ohlin model and distribution of gains and losses from trade

Let me briefly introduce the Heckscher-Ohlin model of the gains and losses from international trade. While it is not clear that empirical evidence confirms the model, it is nonetheless useful for reasoning about trade. I present the conclusion of the model, but do not run through the argument for these conclusions¹⁹. I begin by explaining the concepts of **intensity** and **abundance**.

Suppose both goods G and H use two inputs of production, K and L (capital and labour). At given prices for K and L, production of a unit of G will likely use the inputs in a different ratio to the production of a unit of H. Suppose that at any given input prices, G always uses a higher ratio of K to L than does H. This makes the production of that good *K-intensive*. Note that intensity is a *relative* concept to do with the ratio of inputs used. In this model, if G is K-intensive, this must mean that H is L-intensive.

If country X's endowment of inputs of production is composed of a higher ratio of K to L than country Y's, then X is *K-abundant* and Y is L-abundant. Again, this is a relative concept. Country X may have a larger absolute quantity of both inputs K and L than does country Y, but, obviously, it cannot have a larger ratio of both K to L and of L to K than country Y.

If country X is technologically advanced and country Y is not, it is likely that the former has a comparative advantage in the production of a technologically intensive good.

However, the Heckscher-Ohlin model makes a prediction about comparative advantage and the direction of trade flow even in cases where technology is assumed to be the same in the two countries in the model. The model makes the following four predictions.

A country will tend to export products which are intensive in factors that are possessed by the country in abundance. So, for example, a country that is labour-abundant, such as a developing country, will tend to export products that are labour intensive. That is: country Y, which is L-abundant, will tend to export the labour intensive good H.

As it does so, the relative price of the abundant factor in that country will rise. To continue with our example, the developing country will see the price of labour rise relative to the price of capital - wages will rise relative to the rent. Suppose w is the factor price for L and r is the factor price for K. Country Y will see the ratio w/r rise. Real wages will rise and real rents will fall for *both* the labour intensive good and the capital intensive good.

¹⁹ For a fuller introduction to the model, see standard textbooks on the economics of international trade such as Krugman and Obstfeld (2003) (in particular the chapter on the Heckscher-Ohlin model).

Moreover, the purchasing power of owners of labour (labourers) will rise and the purchasing power of owners of capital will fall. In the initial discussion of comparative advantage, international trade turned out to raise the aggregate product. With this latest prediction of the Heckscher-Ohlin model, there are reasons for thinking that the *distribution* of gains from international trade will be uneven. There will be some gainers and some losers from trade. According to the model, owners of labour will gain in country Y and owners of capital will lose. Its trade partner, which we might think of as a developed country, is capital abundant and tends to export the capital intensive good G. In X, owners of capital will gain and owners of labour will lose.

Finally, *international trade will tend to equalise the relative prices of the two factors in the two countries.* That is, the ratio w/r in country X and the ratio w/r in country Y will tend to equalise.

The theory of comparative advantage suggests that with specialisation and international trade, aggregate global product will increase given constant amounts of factors of production and technology. For each country, there is an increase in average efficiency. Even if some industries unable to compete with imports are destroyed, the human and capital resources thus freed up can be absorbed into production in some other industry where the country has comparative advantage and in which it now specialises. Since the country has comparative advantage in this latter industry, the resources have moved from low-productivity protected sectors to high-productivity export sectors.

Trade can potentially open up a foreign market, boosting demand for domestic products. Domestic producers can expand their production to satisfy this larger demand and even achieve economies of scale in the process. Trade liberalization can mean that imported inputs used in the production of domestically produced goods are cheaper, thus reducing domestic cost of production. Liberalization can result in greater competition from foreign firms in the domestic economy. This can lower prices and force improvements in efficiency in the local production. Liberalization can also affect the rate of economic growth by, for example, leading to greater production to meet the greater demand generated by access to foreign markets.

There are both winners and losers in this model. The model predicts that the gains from trade will outweigh the losses. Consequently, the gainers would gain from trade more than enough to compensate the losers for their loss from trade. If the losers could be adequately compensated by the gainers, then everyone would be better off as a result of trade. However, there may be many reasons why the losers from trade are not adequately compensated. Some of these reasons will be discussed in a section below on political aspects of development.

6.2 Rationales for government intervention

6.2.1 Coordination failure: the roles of history and expectations

From the above, it might seem that under free international trade between developed countries and developing ones, the wages of various factors of production will gradually converge (as per the Heckscher-Ohlin model). However, there are reasons why different economies might experience persistently different rates of

investment and why similar rates of savings in two economies might lead to different rates of economic growth. Among the reasons are issues of coordination failure.

An economy may have multiple equilibriums. The market is capable of reaching each of these equilibriums and once it reaches one, it would tend to stay there, unless some force moved it away. The equilibriums may not be equally desirable from society's point of view.

One particular instance of multiple equilibriums is where the economy finds itself stuck in a relatively low level equilibrium because of a *coordination failure*. If a relevant set of agents could coordinate their actions, the economy would move to higher level equilibrium which is better for the economy and the agents concerned. However, in the normal course of things, the agents fail to coordinate and the market remains in the lower level equilibrium. This is one type of obstacle faced by developing countries wanting to develop. It also highlights the role of history in the amount and type of investment that an economy receives today.

Consider a developing country that is largely reliant on its primary sector. Primary products are generally those obtained directly by transforming natural resources. Agriculture, fishing and mining are examples of primary sectors of economies. This contrasts with the secondary sector of economies which involves processes such as manufacturing and construction where primary products serve as inputs. Suppose the country would like to develop an export sector for manufactured goods. There is abundant labour who could be employed in manufacturing and there are entrepreneurs with sufficient resources in terms of finance and know-how to set up the industry. Nonetheless, there may be other obstacles to a move to the 'manufacturing-export-equilibrium' and the economy may remain at the lower level primary sector equilibrium. For, various *complementary* developments that make a manufacturing export sector viable may be absent. The machinery required for the manufacturing industry might require a steel industry which in turn requires iron, mining and coal industries. Yet, these latter industries may not exist, as there is insufficient demand for their products. *If* the manufacturing sector existed, there would be sufficient demand for steel and thus a reason for an entrepreneur to set up a steel industry. In the absence of a manufacturing industry, there is no reason for an entrepreneur to establish a steel industry, as there is no demand for the product. Similarly, *if* the steel industry existed, there would be sufficient demand for iron to warrant establishment of an iron industry. A similar story can be told for the coal and mining industries which create inputs for iron production.

At one end, the entrepreneur who contemplates setting up a manufacturing industry sees an absence of inputs of production in the economy. Meanwhile, at the other end, the entrepreneur sees insufficient demand for the manufactured product. The incomes and preferences of workers in the developing country may not be sufficient to generate adequate demand for the manufactured goods to warrant the initial setup costs. The entrepreneur would have to sell the products overseas. Yet, in order to do so, the economy must have adequate railways to transport the goods to a port and a shipping industry to ship the goods from the port to foreign markets. The railway and shipping industries, in turn, do not exist because there is insufficient demand for their services and insufficient inputs for their production. Demand for their shipping services would come from an export sector (like manufacturing) and demand for railways would come from industries like manufacturing or iron (to transport coal to iron producers). Inputs for railways and shipping would include steel

and coal. These sorts of forward and backward linkages abound in developing economies (Hirschman 1958). The steel industry facilitates development of railway industry by increasing availability or lowering price of steel. This is a *forward linkage*, affecting the ease of supply of another product. The steel industry has a *backward linkage* to the coal industry, as expansion of the former raises demand for the latter.

Note that any one entrepreneur may be unwilling to invest in establishing a mining, coal, iron, steel, manufacturing, railway, or shipping industry. This may be because she is uncertain that there will be demand for her product. Or it may be because she is uncertain whether inputs of production for her industry will be available cheaply. None of these industries is viable on its own. Yet, they are collectively viable, if only the entrepreneurs contemplating investment in each industry could coordinate and rely on the others to invest. Unless this *coordination failure* is resolved, the economy will remain at the lower level equilibrium.

Note this link to the section below on dynamic comparative advantage. Static comparative advantage might move a country into specialising in a product given the existing low level equilibrium. Yet the country's dynamic comparative advantage may be in some other specialisation that is not reached by the market because of coordination failure.

Thus, history plays a part in explaining why different economies might experience persistently different rates of investment and why similar rates of savings in two economies might lead to different rates of economic growth. A country with a well established industrial sector, with a variety of industries, will attract investment for establishment of new industries. The existence of complementary industries makes it profitable for entrepreneurs to invest in this economy to set up new industries. Many developed countries are like this. On the other hand, a developing country which has very little industry and, in particular, lacks various key industries, will be unattractive to investors. This is the case not only for foreign investors, but also for domestic savers. A similar rate of savings to the developed country may still yield different rates of economic growth of the two economies. Domestic savers in the developing country will be unwilling to invest in their economy for the reasons above and this will affect the rate of economic growth. Meanwhile, domestic savers in the developed country will be eager to invest in their economy because complementary industries exist and their investment is more likely to be profitable.

6.2.1.1 Remedial policies for coordination failure

In cases of coordination failure, each potential investor bases her decision on her expectation of whether other investors will invest in complementary industries in a given time period. No investor wants to be the first to make the move, because the first will face losses for at least the short run while other investors set up other industries that have linkages to the pioneering investment. The first investor's action would have positive externalities – making it profitable for others to set up complementary industries – but brings poor returns to the investor herself, at least in the short run.

One way to deal with this is government action. The state can be the first actor, willing to bear some losses for the sake of the positive externalities. The state seeks out the key sectors – call them leading sectors – whose development would spur the development of complementary sectors through forward and backward linkages.

Backward linkages usually have direct consequences by raising demand for inputs. Forward linkages generally have more diffuse effects. They increase supply of something which is an input for many things, so that investment in any one of them rather than in others is not assured. Moreover, the input will be only one input among others for the other product and if prices of other inputs stay the same, the effect of lower price of one input may be small. Sectors that have been thought to be *leading sectors* in this sense include heavy industry, exports, tourism, transportation and agriculture.

If the government invests in a leading sector, preferably a very low profitability sector (in which private entrepreneurs would therefore be unlikely to invest), it can change the expectation of entrepreneurs. Without government action, each entrepreneur expected that no private investor would make the first move (as this would not be profitable in the short run for any investor). Accordingly, no entrepreneur was prepared to make a move in the future. With government action, entrepreneurs expect that, in the future, there *will* be some complementary industry necessary for the profitability of their own enterprise. Therefore, entrepreneurs will be more willing to undertake the investment.

6.2.1.2 Capital markets

Opponents of government action grant that the government action could resolve the coordination failure, but argue that it is not the only – nor the best – way to do this. The problem is that the first mover would face losses in the near future. However, it may well be profitable in the longer run as complementary industries set up to take advantage of the linkages created by the first mover. Accordingly, first movers should be able to borrow against their longer-run expected profitability to tide them through their short run losses.

In many developing countries, credit markets may be poor and so first movers may be unable to find a willing lender. This is indeed a market failure and could justify remedial government intervention. However, many would argue that the appropriate role of the government would be to fix the credit market and not to set up the leading sector as a public enterprise. This is in keeping with the rule of thumb that it is best to deal with a market failure as *directly* as possible, as less direct policy tends to lead to unintended distortions of incentives elsewhere in the economy (Krugman and Obstfeld 2003: 227).

This does not seem to be the end of the matter, however. Research in the implications of asymmetric information suggests that in many cases it may be best to see capital market imperfections as inherent and not simply something that governments can fix (see Stiglitz and Weiss 1981). Banks would have to be willing to lend to a firm that sells its product below cost in the hope that it will eventually increase productivity enough to become a viable competitor. This would be highly risky for a bank, which is at an *information disadvantage* in judging the credibility of the firm's pronouncements about its own future profitability despite current losses. This situation of asymmetric information is an inherent feature of the operation of economies. Once we take seriously the intractability of these capital market imperfections – rather than supposing them to be easily remedied by government intervention – government protection may be optimal (Stiglitz and Charlton 2005: 32).

6.2.1 Increasing returns to scale

Expansion in the scale of production often reduces the average unit cost of a product. These lead to increasing returns to scale. To realise gains from increasing returns there must be a sufficiently large market for the product. If the market is small, a profitable product may never make it onto the market. It may be that if increasing returns to scale are not realised, then the cost (and thus price) of the product will remain too high for potential consumers.

For instance, there may be a close substitute which is of inferior quality but which has complete market share. Given the market share, its producer can realise increasing returns to scale and thus sell the product at a relatively low price. The innovative producer of a substitute which is of higher quality may be unable to break into the market because potential consumers will not immediately shift from the inferior to the superior product. Consumers need time to find out about a product, to build trust in it from seeing others buy it, to be convinced out of brand loyalty or habit or to wait for the inferior product to wear out before they buy a new one. In the short run, the superior product will have only a very small market share and the inferior product will retain its dominant position. This means that the superior product sees insufficient demand to warrant increased scale of production. Accordingly, it does not experience increasing returns to scale and cannot reduce its price to come close to the cheaper inferior product. This higher price further disadvantages the superior product.

Increasing returns to scale in an industry might mean that an 'infant industry' in a developing country cannot compete against import from established foreign producers. Government protection from such imports can allow the infant industry to become more competitive.

6.2.3 Learning by doing

Sometimes assimilation of new techniques of production is possible only through ongoing production at a sufficiently large scale. There may also be increased productivity merely from increased labour skills arising from accumulated experience rather than from any change in technology (sometimes referred to as the Horndal effect). The learning process may also involve innovation which improves the quality of a product or the efficiency of its production. For instance, a type of circuitry may have been designed in foreign conditions where heat and humidity are not a big problem. Use of the circuitry may be sub-optimal in the greater heat and humidity of the domestic environment. Domestic producers can innovate and modify the product to cope with the different conditions (Ray 1998: 669).

Learning by doing may not be possible for an industry if it must face import competition that already has the benefits of having learnt from experience. A government may want a domestic industry to achieve the benefits of learning by doing and thus become more competitive. It may protect the industry from imports in order to give it time to learn.

6.2.4 Dynamic comparative advantage

The existence of increasing returns to scale and learning by doing can mean that an industry is unable to compete against imports from established foreign producers. However, the theory of comparative advantage suggests that there will always be some industry in which the country would have comparative advantage and thus where it could competitively produce.

Why, then would a country want to develop an industry which is outside its area of comparative advantage rather than letting free trade guide the country to its area of comparative advantage? To answer this, it is useful to distinguish static and *dynamic* comparative advantage. There may be industries in which a country does not *currently* have comparative advantage, but in which it *could* have comparative advantage in the future. In such cases, free trade is likely to lead the country towards a specialisation which may be worthwhile in the short run, but which may not be best in the long run.

One reason attaches to the existence of *positive externalities* of the operation of specific industries that do not attach to the operation of other industries. Positive externalities are a sort of market failure in which the market equilibrium produces less of a good than is socially optimal. In our case, the market may fail to promote an industry even though, from a social optimum point of view, it is highly desirable. From this latter point of view, the particular industry may be judged to generate more advantages in the long run than the area of (static) comparative advantage would generate.

Here are some examples of such positive externalities. The growth of some industries prompts other developments in the country. For instance, it might spur a local industry for intermediate inputs, as I mentioned in the section on coordination failure. It might yield knowledge and technical expertise that can spill over into other industries within the country as employees eventually leave one industry for another. It might lead the government to improve key infrastructure necessary for the industry to prosper (such as roads or electrification) or institutions (such as intellectual property law or bankruptcy law) to assist the industry if it is sufficiently important to the economy. Depending on the level and type of inputs and technology involved in the industry, this public expenditure can promote various sorts of specialised technical education or improve telecommunications infrastructure and so on.

In these ways, the industry in which a country specialises can affect the development of the country not merely in increasing its income through the income directly generated through exports, but also through flow-on effects (i.e., positive externalities) that pave the way for other industries to establish themselves. While the area of static comparative advantage would maximise export receipts in the short run, some other industry may turn out to be preferable in the long run.

Another reason a country may want to develop an industry other than that of its static comparative advantage relates to the fact that, for many developing countries, the area of comparative advantage lies in primary sector areas such as agriculture and mining. It is an established empirical observation that as consumer budgets grow, consumers spend a decreasing proportion of their budget on primary products such as foods²⁰. A greater proportion is spent on luxuries rather than necessities and many sorts of primary products fall under the latter classification rather than the former. A greater proportion is also spent on processed goods. As income grows, the demand for primary products is likely to grow, but will do so at a decreasing rate.

There is a tendency for developing countries that export mostly primary products and import the bulk of their manufactured goods, to see their terms of trade (the price of a country's exports divided by the price of its imports) decline. Other

²⁰ With food items in particular, this behaviour is known as Engel's Law.

contentions in the literature include the claim that primary product prices tend to fluctuate widely. If this is the case, it may contribute to economic instability of countries which rely on the primary sector.

Suppose the export sector of a developing country is heavily dependent on primary products. One way for the country to increase its national income is to simply try and sell more of the primary products. However, there is a limit to how far it can grow its share of the market in these products.

Another way for it to increase its income is to move into an industry further along the production chain that transforms primary product into final product. Suppose country A exports raw wool (a primary product) to country B which processes and dyes it and makes woollen clothing from it. Consider this clothing as the final product, a product which is not used as input in any further production process. If country A begins to process its raw wool rather than exporting it, it can enter a new market: that for processed wool or for dyed wool or woollen garments.

Country A can increase its income in this way for the following reason. Consider the value of the final product of the woollen garment to be an amount Z . Amount Z can be analysed into component amounts of value added at the various steps in the chain of its production. The raw wool has a value of V , the processing and dyeing of the raw wool adds a value W , making the processed wool into wool cloth adds a value X and making this cloth into clothing adds a value of Y , where $V+W+X+Y=Z$. If country A exports the raw wool, its income is V . If it exports at a later stage in the chain of production, its income is the increased amount $V+W+\dots$. This strategy for greater economic growth and development is known as moving up the value-added chain towards *higher value added* production.

If a country expects that in the long run, a specialisation in manufacturing is more lucrative or stable than a specialisation in a primary sector, it might promote more capital- and technology-intensive industries in which the country does *not currently have a comparative advantage* but in which it *could* become competitive.

6.3 Types of activist trade policy: Import substitution and export promotion

We have seen some reasons why governments might want to *actively* promote particular industries through policy. Import substitution and export promotion are two sorts of policies countries can follow to promote industries. Both methods distort market outcomes and both involve significant government intervention.

Import substitution involves barriers to imports, perhaps coupled with government support for the import-competing sectors. The aim is to let the import-competing firms become established and become competitive. They can become more competitive by, acquiring organisational experience, increasing returns to scale, building relationships with suppliers of inputs in order to get these at a low cost, developing new technology or techniques particularly adapted to the domestic market and so on.

Suppose a local substitute for a currently imported product is just as good or better (more suited to local conditions). Suppose also that the product type has increasing returns to scale, such that it is difficult for the fledgling domestic import-competing producer to sell at sufficiently low prices to compete with the imports. Import protection can be used to reduce the share of imports in the relevant market

and thus leave more of the market for the domestic producer. This can allow the latter to increase its scale of production and may help it become more competitive by gaining other advantages such as experience. The hope is that the domestic producer will eventually become competitive enough to survive without protection.

Export promotion involves government promotion of exports. Means of doing this include subsidies for inputs and for production, cheap access to imported inputs (perhaps through import quotas reserved for selected exporters) and preferential credit at below market rates to facilitate borrowing for investment.

Developed country consumers generally would prefer developing countries to adopt export promotion than import substitution, as the developed country consumers would thus have access to cheap imports from these countries. Moreover, export promoting countries tend to have fewer import barriers than import substituting countries. This is attractive to developed country exporters who may want to access the markets of certain large developing countries.

For the developing countries themselves, import substitution can lead to entrenched business interests in the import-competing sector who take for granted the government protection from cheaper imports. They may not believe that this period of support by the government is limited. Accordingly, they might see no reason to take advantage of the period of shelter from competition to become more competitive. They may never become sufficiently competitive as to be able to survive without government protection. Then the business interest acts simply as a drain on government money and domestic consumers face higher prices with no compensating benefit.

Note that for a protected industry to become competitive, it may need access to a large market. The industry cannot reach a sufficient scale of production to benefit from increasing returns and falling average cost of production if there is not sufficient demand for its product. For many developing countries, the domestic market may not be large enough, meaning that the industry needs to access export markets to become more competitive. This leads in the direction of export promotion policies. Some of the government protection for the fledgling domestic industry might continue, but one sort of support – namely import barriers to stop foreign competition – is no longer on the cards. Exporting to a foreign market involves competing against foreign producers. Export promotion is preferable to import substitution for many developing countries, as it allows access to larger markets.

There are other reasons why export promotion is desirable. A developing country may need income, for example to service international debt. Greater export earnings are a way of doing this.

6.3.1 Effects of tariffs and of export subsidies

Suppose a developing country imposes a *tariff* on an import. This will raise the price at home. This hurts domestic consumers and benefits domestic import-competing producers. The government also receives tariff revenue, boosting its ability to spend. There is an efficiency loss as domestic producers produce more than they would and domestic consumers consume less than they would under an efficient market equilibrium.

Assessing the overall wisdom of the tariff depends on distributional features and on the social importance placed on a dollar of cost or benefit accruing to different

groups. For instance, it matters whether the producer gain accrues mostly to wealthy owners of resources or to low wage workers. It matters whether the consumer loss is borne mostly by poorer than average people or by the affluent. It also matters whether the government puts its tariff revenue to good use. These are effects in the short run. There may be other relevant effects in the longer run. We have come across these effects in previous sections. The import-competing industry may be an infant industry which needs only temporary protection and which may promise future benefits which outweigh the costs of the protection. These benefits may be in the form of externalities for the rest of the economy or in the form of a surer and more stable source of export revenue in the future.

Consider an export subsidy. The subsidised exporters in the exporting country experience a rise in the price received. If the exported good is also sold on the domestic market, then the price faced by domestic consumers may also rise. Producers would prefer to sell at the higher price overseas than sell domestically at a lower price, and would need to be enticed to sell domestically by a rise in domestic price. The government loses as it must foot the bill of the subsidy. There is an efficiency loss as domestic producers produce more than they would and domestic consumers consume less than they would (as they may face higher prices) under an efficient market equilibrium.

Again, the wisdom of the subsidy depends on things like distributional effects, externalities and potential long run effects. As we have seen in previous sections, a well thought-out export subsidy can allow an infant industry to establish itself and to become a competitive export earner in the long run. There may also be positive externalities such as rectifying coordination failures and moving to a better market equilibrium if multiple equilibria are on offer. Moreover, if the consumers who lose at home are affluent and the producers are mostly low skill workers, then these results become more acceptable.

Let me note the effects of these measures for trade partners. The producer in the trade partner country X, facing an import barrier, experiences a fall in demand as the tariff raises prices for consumers in the importing country Y. Depending on the size of Y's market for the relevant good relative to the size of world market, country X will also undergo a change in price of the good. If Y has a small market, then the tariff makes very little difference to world price and consequently to price in X. If Y has a large market relative to world market, then the price in X will fall by some amount smaller than the size of the tariff. So, producers in X face a fall in revenue as demand for the product falls. Consumers in X will benefit from a fall in price if Y is a sufficiently large market, but will face no effects otherwise.

In the long term, if the import-competing producer in Y ceases to be an infant industry and grows up to become competitive, then the producer in X will face grater competition in the world market and may even see its market share shrink.

In the case of an export subsidy by country Y, the importing country X undergoes a fall in price. Consumers in X benefit and the import competing producer in X finds it harder to compete and, if the subsidy is substantial enough, could be driven out of business.

6.4 Expected distributions of gains and losses in various types of international trade

6.4.1 Trade between a developed country and a developing one

Recall that the Heckscher-Ohlin model predicts that the relative prices of factors of production will tend to equalise across trading partners. If a developed country trades with a developing one, we expect the former country to export a capital intensive product and the latter to export a labour intensive product. The model leads us to expect that owners of capital will become wealthier in the developed country and less wealthy in the developing country. Similarly, we expect that the owners of labour (labourers) will become wealthier in the developing country and less wealthy in the developed country. Conditions of production are so different in the two countries, that there should be plenty of gains. Labour in the developing country can expect a rise in wages and consumers in the developed country can expect much cheaper goods.

Yet, the large differences in conditions of production also mean that distributional effects of free trade between such countries are likely to be large. Gains to consumers from much cheaper imported products are expected to outweigh the losses to specific small groups. However, those who stand to lose in a developed country often organise themselves to oppose free trade with a developing country. Fear of a fall in real income and of losing jobs has led to US protection of particular sectors such as the auto industry, agriculture and textiles. (Krugman and Obstfeld 2003: 228-32).

While specialisation according to comparative advantage can increase the aggregate income of both countries, the pattern of specialisation may nonetheless be problematic. This is for reasons familiar from our discussion of dynamic comparative advantage and of complementary industries. The developing country may experience an expansion of low-skilled labour-intensive industries as competing industries in the developed trade partner shut down and relocate, but at the same time the developing country experiences a flight of some technically intensive industry to the developed country. This may be because the latter country may have better infrastructure and easier access to high-technology inputs and other complementary industries than does the developing country. The developing country may be unhappy with this division of specialisation.

While talking of developed and developing countries, as I have thus far, is fine for explaining many features of development economics, the dichotomy is too simplistic for many other matters. This is one such instance. It is important to differentiate between developing countries at varying stages of development, and with varying degrees of wealth. The divide between the Least Developed Countries (LDC) and the middle-income developing countries can be substantial. Some developing countries will have better infrastructure than others. Suppose trade between developed and developing countries includes not just two countries, but three – a developed country, a middle-income developing country and an LDC. The existence of better infrastructure and complementary industry in the middle-income than in the LDC may mean that investors relocate some low skill labour intensive industry to the former rather than the latter. This may be despite the latter country having lower wages, as wages are only one component of cost of production.

6.4.2 Trade between two developed countries

We can expect that developed countries have depth of product variety and that any differences in proportions of various factors of production will be relatively small. For these reasons, distributional effects will be small and we can expect fewer impediments to trade between such countries. Indeed, the EU is an example of such trade.

Much of their trade might be in similar, but *differentiated*, products or in goods that do not use substantially different proportions of factors of production. Similar products can be differentiated in terms of features like branding. The main effect for such trade may be a bigger market without a drastic change in factor prices. Here trade is more likely to bring *actual* Pareto improvements.

Suppose one developed country produces only white wine and another produces only red. Suppose consumers in both countries want to try both kinds of wine. Free trade allows each country to keep half its domestic wine and export the other half. Consumers have more variety and producers do not have to downsize in either country. It seems that no one stands to lose from trade in this case. The only opposition might be if there is monopolistic or oligopolistic production in autarky (a situation of no international trade). In a situation of monopoly, a producer can charge higher prices, because consumers have no other producer to turn to. The monopolist will want to resist free trade as the resulting entry of competing producers into the domestic market will lower prices and reduce the profits enjoyed by the monopolist under autarky.

6.4.3 Trade between two developing countries

The optimistic result for free trade in the previous case required two factors: (i) similar per capita income (so that products demanded are similar and thus unlikely to vary much in terms of factor composition) and also (ii) a certain depth of consumption or input variety. Developing countries can satisfy the first criterion, but they fail the second.

Such trade can serve the need to access a larger market than would be possible under import substituting industrialization: producers now access export markets as well as the domestic market. Suppose two developing countries open free trade between themselves. They were import substituting before and are now jointly import substituting. This allows them a bigger market. If the industries simply located in one country each, cutting out duplications and thus reaping returns to scale from the larger market, they could be more successful.

However, there is no reason to expect such harmony where each major industry picks one country, so that each country has one major industry. If one of the countries is larger or has better infrastructure or better access to skilled workers, it would end up with both industries and the other would be left with none. The more similar the countries, the more likely that the location choices of industry will be evenly distributed. However, increasing returns mean that even a small advantage can magnify over time, through a process termed *agglomeration*. The process involves a chain of activities in which each additional link heightens the prospects of a fresh link to be forged.

Locational choices are like this. Recall the earlier discussion of complementary industries with regard to the problem of coordination failure. The

absence or presence of complementary industries can influence an entrepreneur's decision to invest in a region. A slightly better climate for industry can prompt the location there of one industry. This makes it more likely that fresh industries will locate there and so on (Ray 1998: 740-2)²¹.

This concludes my presentation of the economic background presupposed for the case study. In chapter 7 I discuss the WTO.

²¹ For an assessment of broader issues surrounding trade between developing countries and in particular regional trade agreements among such countries, see (UNCTAD 2007: ch IV D)

Chapter 7: The World Trade Organization

I discuss the World Trade Organization (WTO) in relation to egalitarian concerns about global poverty and under-development. I explained at the start of chapter 6 the relevance of international trade to development and global poverty. Let me build on that explanation by outlining the connection of the WTO to development and global poverty. I revisit points from the previous chapter about interventionist trade policy as a way to promote infant industries (section 6.2) and about the distribution of gains and losses from trade (section 6.4).

In the previous chapter's discussion of the likely distributions of gains and losses from international trade between developed and developing countries, I noted that such trade is expected to lead to gains to labour in the developing countries and losses to labour in the developed countries, and gains to capital in the developed countries and losses to capital in the developing countries. It is expected that the relative factor prices across trade partners will move towards equality.

Yet, it is also desirable for developing countries to move up the value-added chain and diversify their economies to have a greater component of capital intensive and high-skill-intensive production. Interventionist trade policy is a means of doing this. In general, well-executed interventionist trade policy can potentially increase national income; foster the construction of new infrastructure and services in the country; encourage the inflow of technology and know-how; and diversify an economy, dulling the effects of economic shocks.

Note that if many developing countries move up the value-added chain and trade competitively in such production, the developed countries will experience a fall in returns to the factor of capital as well. Developed countries are already uncompetitive against developing countries in areas of developing country comparative advantage (such as labour intensive goods). If developing countries are allowed to cultivate areas of dynamic comparative advantage, then the developed countries may suffer losses without compensating gains. Both the returns to labour and the returns to capital would increase in the developing countries and would fall in the developed countries. Recall that factors such as coordination failure are among the reasons that developing countries are unattractive to entrepreneurs (section 6.2.1). Well-executed development policy could overcome problems such as coordination failure and attract more investment to a country. In effect this is a path towards greater wealth redistribution. It includes both income redistribution from the equalization of factor incomes for labour and capital, and movement of investment from developed countries to developing, as the latter become increasingly attractive for entrepreneurs.

The WTO sets rules for international trade. These rules impinge on the ability of governments to set certain types of development and trade policy. This is not objectionable in itself, as some of the rules, and certainly the overall framework of a stable system of rules for international trade, are desirable. However, since the rules affect international distribution of wealth, they should be investigated as potential tools for progressive redistribution and poverty alleviation.

In this chapter, I describe some of the 'special and differential treatment' (SDT) the WTO rules allow for developing countries, and the reasons for such treatment. The reason for the SDT is not wealth redistribution, but to make allowances for the different needs and capabilities of developing countries. Against the backdrop of existing SDT, I consider another proposal for preferential treatment

of developing countries. This proposal also makes allowances for the different needs and capabilities of developing countries, and addresses some of the criticisms of existing SDT. However, the main reason I examine this proposal is because of its potential for radical progressive wealth redistribution. The proposal I consider is the Market Access Proposal (MAP) advanced by Joseph Stiglitz and Andrew Charlton.

There are many ways of reforming WTO rules to benefit developing countries, and all of these would be of interest to the egalitarian. They range from smaller, but more politically likely changes, to radical, but less political likely ones. I only consider one proposal, the MAP, and it is closer to the latter end. I advocate it in the sense that I think it would further some important egalitarian aims. However, I do not argue here that it is feasible or that, given likelihood of implementation as a criterion, it is the proposal most worthy of political effort on the part of egalitarian activism and advocacy. These are issues which a fuller egalitarian investigation of the issue would have to consider. The criticisms of SDT in section 7.4 suggest some smaller, but nonetheless important, and more likely reforms.

There is a reason I focus on the MAP. It is a radical enough proposal to illustrate the potential for international trade to mitigate global poverty and under-development. The fact that trade can play a part in development is widely acknowledged across the political spectrum. Some might note the potential in terms of an indefinitely long-run effect supposed to eventuate from laissez-faire free trade (but note the rationales given in the previous chapter to doubt the efficacy of laissez-faire free trade and to instead argue for government intervention). The MAP instead notes a political decision which is likely to make a substantial difference in the relatively short to medium term. Such a reform is technically on the cards, whatever might be thought about its political likelihood.

In section 7.1, I describe the purposes and powers of the WTO. In section 7.2, I describe preferential treatment of developing countries under WTO rules. Section 7.3 lists reasons for preferential treatment. Section 7.4 turns to criticisms of the existing SDT.

Section 7.5 introduces the Market Access Proposal advanced by Stiglitz and Charlton. Section 7.5.1 connects the proposal to the criticisms of existing SDT noted in section 7.4, and also to the WTO's reasons for implementing SDT. Section 7.6 relates the MAP to the egalitarian perspective.

7.1 The purposes and powers of the World Trade Organization

The WTO was established in 1995 as the successor of the General Agreement on Tariffs and Trade (GATT) which was created in 1947. Much of the GATT agreements on trade were carried over into the WTO, though there have been changes and additions in rounds of negotiations since then. Let me list the purposes that the WTO sets itself and the main principles by which it guides itself. I expand on this basic description of the WTO in later sections where I discuss the organization's position on trade and development relating to developing countries in particular.

The declared objective of the World Trade Organization (WTO) is to help trade flow smoothly, freely, fairly and predictably. It claims to do this neutrally, administering trade agreements, acting as a forum for trade discussions and settling disputes, reviewing national trade policy issues through technical assistance and

training programs and cooperating with other international organizations (Peet 2003: 158) (WTO website).

The preamble to the Marrakesh agreement establishing the WTO in 1995 states that the premise under which the members come together to negotiate rules for international trade includes the following: "...relations in the field of trade and economic endeavor should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services, while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development..." (Marrakesh Agreement). This sets the aims of the organization into the egalitarian context of this thesis.

Members of the WTO are party to various agreements that set rules for the conduct of international trade. Part of the reason why such a set of rules is needed is this. The rules provide individuals, businesses and governments around the world with some confidence that there will be no sudden changes to policy in terms of the conditions with which they must comply in international trade. The rules thus have to be transparent and predictable (WTO website). This fosters an environment conducive to greater international trade and is in keeping with one of the aims set out in the Preamble of the Marrakesh agreement establishing the WTO.

The Preamble of the Marrakesh Agreement establishing the WTO also lists the following aims for the organisation. One: a system of trade that allows optimal use of world resources. By promoting specialisation in areas of comparative advantage, countries' resources are put to their most productive uses. Two: to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development. With open access to the richer and larger markets of the developed countries, the developing countries have greater scope to increase their export revenue and thus national income.

According to the Preamble, the organisation pursues these aims by the following means. One: a system of trade that allows for reciprocal and mutually advantageous benefit. The reciprocal benefit consists of a country opening itself up to imports in return for export access to the markets of others. The mutual advantage lies in consumers in two trading countries benefiting from greater competition and lower price as their economies specialise in the direction of comparative advantage. The owners of different factors of production in the trading countries also benefit in ways we expect from the Heckscher-Ohlin model.

Two: raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand. These are to be considered in relation to international trade. If a country can raise national income through greater export revenues, it can improve the standard of living of its inhabitants. Access to a greater variety of commodities than are produced nationally may also contribute to this. Employment can be generated by export industries and can be reduced by import barriers erected by trade partners.

Three: a substantial reduction of tariffs and other barriers to trade and elimination of discriminatory treatment in international trade relations. Removal of barriers to trade allows countries to access larger markets through exports.

According to article III (5) of the Marrakesh Agreement establishing the WTO, the organization also aims for coherence in global economic policy-making with the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD), the latter being one of the branches of the World Bank.

The members of the WTO must adopt certain agreements. The two main principles of these agreements are these.

One, *the Most Favoured Nation (MFN) principle* stipulates that if a WTO member country grants a trade deal, such as lower customs duties, to one trading partner, it must automatically extend that deal to all other WTO member countries. Some exceptions are permitted, but only under strict conditions. The exceptions are as follows: a group of countries may implement a Free Trade Agreement (FTA) which applies only to goods traded within the group while discriminating against goods originating from outside the group; countries can allow developing countries special access to their markets; a country can initiate barriers against products which are traded unfairly from a specific country; with respect to services, countries can discriminate in limited circumstances (Article I of GATT 1947).

Two, the *National Treatment policy* stipulates that imported and locally-produced goods should be treated equally, at least after the foreign goods have entered the market. The same applies to foreign and domestic services, and to foreign and local trademarks, copyrights and patents (items of intellectual property). Since this policy only applies once the good, service or item of intellectual property has entered the domestic market, customs duties on imports are permitted even without an equivalent tax on the corresponding domestically produced item (Article III of GATT 1947).

In working to reduce trade barriers, the WTO can allow countries to introduce changes slowly and usually gives developing countries longer to comply.

The agreements of the WTO apply to three main areas of trade: goods, services and intellectual property. The General Agreement on Tariffs and Trade (GATT) governs trade in goods. The core of this is the GATT agreement of 1947. The WTO is a successor to the GATT arrangement as it evolved over the decades until the 1995 replacement of GATT by WTO. The General Agreement on Trade in Services (GATS) governs trade in services. The Agreement on Trade-Related Aspects of Intellectual Property Rights (Agreement on TRIPs) governs intellectual property.

As can be expected with such wide ranging aims, they sometimes require conflicting policies. In such cases, the relative importance of the conflicting aims or means to these aims must be judged and some compromise must be reached. The provisions for Special and Differential Treatment are an instance of this.

7.2 Preferential treatment of developing countries

The WTO (and GATT before it) recognises the particularly vulnerable position of developing countries and especially of the poorest among these, such as the least developed countries. With this vulnerability in mind, the organization allows some differential treatment of developing countries that does not apply to developed

countries. The Special and Differential Treatment (SDT) provisions of the WTO give developing countries special rights and allow developed countries to treat developing countries more favourably than they would other WTO members. Let me briefly outline the evolution of SDT (Hoekman and Kostecki 2001: Table 12.1).

GATT 1947 Article XVIII acknowledged the special status of countries ‘which can only support a low standard of living and are in early stages of development’ by allowing them to apply some trade restrictions in order to raise standards of living. For example, it mentioned infant industry protection as an additional facility granted to these poor and developing countries (GATT 1947: Article XVIII.2a).

In 1964, the United Nations established the UNCTAD (UN Conference on Trade and Development).

In 1965, a Part IV on ‘Trade and Development’ was added to the GATT agreement. The principles and objectives of this part include the following. It recognizes that export earnings can play a vital part in development and that joint action is essential to the development of developing countries. It notes that the parties to the GATT agreement may enable the less developed members to use special measures to promote their trade and development. It describes paths which may benefit the poorer countries, such as rapid and sustained expansion of exports and diversification of their economies away from an excessive dependence on the primary sector. It notes that the developed countries party to the agreement do not expect reciprocity for commitments to reduce barriers to imports from the developing countries.

However, while Part IV pronounces on various issues of interest to developing countries and describes policies which would benefit them, it does not legally oblige the developed countries to implement the described policies for the benefit of the poorer countries. It contains no legally binding obligations other than to consult.

The Generalized System of Preferences (GSP) scheme was put into motion by the UNCTAD in 1968. It calls on developed countries to grant tariff preferences to developing countries on a non-reciprocal basis. The preferences are granted unilaterally and voluntarily. There is no legal obligation that the preferences be granted, and there are no binding specifications on the areas in which the preferences should be granted.

In 1971, the GATT grants an authorization for the GSP preferences. The waiver is made permanent by the 1979 decision of the GATT known as the Enabling Clause²². The Clause enables contracting parties to accord differential treatment to developing countries as a departure from the MFN principle since it allows that the favourable treatment granted to a group of developing countries need not be extended to other contracting parties. This consolidated the concept of non-reciprocity, where trade concessions made by country X to country Y (say, lowering of tariffs on imports from Y) need not be reciprocated by similar concessions from Y.

²² Officially the “Differential and more favourable treatment reciprocity and fuller participation of developing countries” 1979.

7.2.1 Early years of GATT and the sidelining of developing countries

One attempt at making up for the particularly vulnerable situation of the developing countries was to exempt them from some of the obligations GATT placed on developed country members. This occurred in the early years of the GATT agreement, precursor to the existing WTO arrangement.

In the first twenty years of the GATT, developing countries were given few obligations, but at the same time, they had only a weak voice in negotiations and little power with which to assert their interests.

Article XVIII of the GATT rules allowed poor developing countries to take protective measures against imports. Developing countries could thus be members of GATT, and yet still evade some of the obligations placed on the developed countries. These rules allowed the developing countries greater freedom in determining their developmental policy. However, this advantage came with a cost. The exemptions allowed the developing countries to introduce trade protections at their own discretion. This rendered doubtful any concessions made by a developing country: it could effectively rescind the concession at its discretion. Accordingly, these countries had even *less bargaining power to shape negotiations in their interests* (Stiglitz and Charlton 2005: 43).

Developing countries benefited from liberalization of industrialized countries because of the MFN principle. However, the fact that they could evade many obligations to reduce trade restrictions meant that they only had a peripheral role in negotiations. This resulted in developing countries having little influence on the way that the industrialized countries liberalised. Those with a greater role in negotiations set the agenda according to their interests. They chose to discuss sectors of the economy that were of greatest concern to them, and where they had the most to gain. Liberalization in trade of goods of interest to developed countries occurred swiftly. Yet, liberalization in trade of goods of interest to the developing countries – especially labour-intensive goods – lagged behind and the developing countries ultimately suffered. Had the developing countries had greater influence in setting the agenda for negotiations, they would likely have focused on areas in which they could benefit most from reductions across the world – areas such as agriculture or labour intensive production and manufacturing.

Many developed countries were fine with the peripheral role of developing countries and with the resulting focus of negotiations. The small markets of the poor developing countries were not particularly attractive to these developed countries. Thus, the latter did not mind too much that the developing countries did not make as many concessions in removing their trade barriers. Moreover, the developed countries were glad at the peripheral role of the developing countries as it meant that they were spared the pain of removing their own trade barriers to products in which developing countries have a comparative advantage. The developed countries mostly sought to liberalize trade in those goods that were traded intensively between developed countries as these countries had the most attractive markets (Stiglitz and Charlton 2005: 93, 44).

The result was a system where the trade policies of the developed countries could be said to be discriminatory against the developing countries, even though the MFN was not generally violated. The most serious barriers to trade were erected in goods where developing countries typically had a comparative advantage (for

example, agriculture and various labour-intensive goods), as these countries had little say in setting the agenda of trade negotiations and little credibility to offer in exchange for concessions they might extract from the developed (Johnson 1967: 79).

In 2004, there were once again suggestions (from the EU trade commissioner) that the developing countries might have a “Round for Free”²³. That is, they might have a round of trade negotiations without having to make many concessions. They could thus benefit from the reductions in MFN rates that occurred, without themselves conceding reductions.

This would be undesirable for the same reasons as the undesirability of the sidelining of the developing countries in the early years of the GATT. Whatever other effects the so called Round for Free might have, it would also reduce the developing countries’ power to influence agenda setting and the direction of trade liberalization. An alternative would be if the developing countries were involved in designing the very core of new WTO policy, so they could participate in agenda setting and steer the design in the direction of their interests. This alternative is preferable to the strategy under discussion which simply exempts developing countries from policies which have been drawn up without their interests in mind (Keck and Low 2006: 180).

Moreover, allowing minimal liberalization by poor countries affects not only their developed country trade partners, but also their fellow developing country trade partners. The volume of trade *between* developing countries, or South-South trade, is growing much faster than that of world trade. Developing countries often face higher tariff barriers in other developing country markets than in developed country ones. There is potentially much to be gained for developing countries if their developing country trade partners lower trade barriers to them (Stiglitz and Charlton 2005: 94).

For these reasons, the peculiar needs of developing countries cannot adequately be met through a ‘Round for Free’-type exemption (and resulting exclusion from negotiation) of developing countries from obligations imposed on other countries.

7.2.2 Current Special and Differential Treatment (SDT)

Developing countries currently have a greater role in negotiations relative to the sidelining in the early GATT years. The following are the main types of current SDT measures:

- provisions aimed at increasing trade opportunities through market access (for example, there are exemptions from the MFN principle so that developed countries are enabled to allow greater market access to exports of developing countries);
- provisions requiring WTO members to safeguard the interests of developing countries (these are not legally binding obligations on developed countries, but rather clauses to the effect that ‘developed countries will *endeavour* to be considerate of poor country interest. Here is an example. “The developed contracting parties shall to the fullest extent possible ... give effect to the following provisions: (a) accord high priority to the reduction and

²³ Later renamed the “Round at a modest price” to acknowledge that the developing countries would still have to commit to binding their tariffs in some areas and to participating in negotiations in ‘trade facilitation’ (see Lamy’s speech “Where Next for EU Trade Policy?” delivered in Berlin on 11 June 2004.

elimination of barriers to products currently or potentially of particular export interest to less-developed contracting parties...” (GATT 1947: Article XXXVII.1));

- provisions allowing flexibility to developing countries in rules and disciplines governing trade measures (this can occur in the form of allowing them some choice in whether to implement agreements requiring regulatory or administrative reform);
- provisions allowing longer transitional periods to developing countries; and
- provisions for technical assistance.

Some examples of SDT from WTO agreements are footnoted below²⁴.

The types of SDT that I will mostly focus on are efforts to increase market access for developing countries and provisions requiring developed countries to safeguard developing country interests. This is not to mark these provisions as more important than other SDT provisions, many of which are very valuable. The focus simply reflects my chosen circumscription of the discussion. Greater market access for developing economies is encouraged via differential obligations on removing subsidies or tariffs and via exemptions from the MFN principle. In some cases developing country governments are allowed to maintain domestic support for certain producers even though developed country governments are enjoined to reduce these²⁵.

Exemption from the MFN principle enables developed countries to lower tariffs on imports from developing countries without also offering the same reduction to like imports from other countries.

The idea is that even if a developed country is unwilling to lower its trade restrictions on imports of some product across the board, it may be willing to lower those restrictions on imports of that product *from developing countries*. The *preference margin* is the difference between the tariffs set on imports from the selected developing countries and that set for other countries (which can be referred to as the MFN rate). The longer term aim is the reduction of MFN tariff rates towards zero (as per para 3(b) of the Enabling Clause). The preferential treatment is intended as temporary and lasts as long as MFN rates are above zero.

7.3 Reasons for Special and Differential Treatment of developing countries and especially of Least Developed Countries (LDCs)

Let me list four different sorts of reasons presented in support of special and differential treatment or SDT (Page and Kleen 2005: 6-8).

²⁴ Here are some illustrative examples from WTO agreements. Regarding leeway in domestic support reduction for the developing countries, see Part IV Article 6.2 of the Agreement on Agriculture. On longer time periods for tariff reduction, see Part IX Article 15 of the same and Agreement on the Application of Sanitary and Phytosanitary Measures Article 10.2. On technical assistance to developing country members in implementing agreements, see Agreement on Technical Barriers to Trade Article 12.7. Some general instances of SDT clauses are these. Agreement on Subsidies and Countervailing Measures Part VIII Article 27; Agreement on Textiles and Clothing Article 6.6.

²⁵ See for instance Agreement on Agriculture Part IV Article 6; Agreement on Subsidies and Countervailing Measures Part VIII Articles 27.2-3;

First, consider the original justification, which was informed by Prebisch 1950 and Singer 1950, and which lies at the foundation of the United Nations Conference on Trade and Development (UNCTAD) and in the adoption of Part IV of GATT. The justification is that developing countries are different in ways that policies best for developed countries are not necessarily best for the developing. These latter countries need to transform the structure of their economies rather than merely expanding the existing structure. The sort of structural transformation involves, for example, promoting particular sectors of the economy in order to develop fluency in more technology-intensive industries. This can require planning and intervention by the government, as well as some temporary loss in efficiency while the intervention in the market bears fruit. Further, developing economies often differ in sectoral composition and in the size and competitiveness of firms. As a result, the argument goes; policies may have different effects to what would be expected in developed countries. There may be lower gains from trade than would be expected for a developed country. Or there may be lower efficiency cost of subsidies (the loss in efficiency caused by the introduction of a subsidy). The idea that developing countries need to intervene more than developed countries need to is the basic argument behind SDT designed to allow developing countries to follow different policies.

Two, trade liberalization can require costly economic and institutional adjustments. For example, developing countries often need to expand production in an export sector or need to enter new foreign markets and there can be substantial costs to making these economic adjustments. To help developing countries make these adjustments and to make the costs more bearable, rules can be modified or transitional rules can be implemented. Ensuring that countries are subject to lower tariffs in a transitional period can make the cost more bearable. The idea is that this will put them on par with (rather than give them an advantage over) domestic producers in the importing developed countries. Even if they do have an advantage over the import competing firms in the developed country, the exporting developing country firms are often too small to make much of a difference to the competitors.

Other substantial costs can be in terms of development of the requisite infrastructure of laws, regulations and policies. Developing countries will probably need to make the biggest changes to comply with the so-called 'Singapore Issues'. The Singapore Issues refer to a group of topics discussed during the 1996 WTO Ministerial Conference at Singapore. The topics include investment protection, competition policy, transparency in government procurement, and trade facilitation. There are heavy costs attached to the creation and enforcement of new competition policy, investment regulations, and trade and customs procedures. Generally, developing countries have the furthest to go to meet these regulation and procedural standards, and often face a shortage of the requisite legal, administrative, bureaucratic and other expertise to design and implement the changes.

Three, many believe that developed countries have benefited disproportionately from past GATT rounds as well as from present WTO arrangements, and that they do so at the expense of developing countries. SDT is seen as a way of redressing the balance. There is evidence that developing countries, particularly the LDCs, had few economic gains and suffered some losses from the Uruguay Agreement (the round of negotiations ending in 1994) of the WTO (see, for example, Page and Davenport 1994). This is due in part to some distortions in the existing WTO system. For example, there is greater protection in sectors like agriculture and textiles – where developing countries have the comparative advantage

– than there is in sectors where the developed countries have the comparative advantage. Even some of those who think greater and freer trade is beneficial to all, might think that such existing distortions need to be offset by preferential treatment for developing countries. These measures can be supported either as a second best economic solution or as a confidence-building measure to include the developing countries despite perceptions of an unfair distribution of advantages from previous rounds of negotiations. Supporters of this view can retain free trade as the ultimate objective, whilst acknowledging that if the protectionism of developed countries prevents us from getting there in the immediate future, then we can at least encourage lower trade restrictions for those most in need of the benefits of trade and those too small to raise protectionist fears (namely, developing countries, especially LDCs and small countries).

Four, some reject the basic premise of GATT, which is that all countries can gain from trade, and argue that some types of countries need different policies. The view is that some countries need permanent special treatment because of peculiar features such as their size or geography. The view holds that many of the poorest countries, or countries that gain least from trade, are not just less developed, but are unable to follow the same path as other developing countries. Such countries may be too small to diversify away from dependence on one or two export commodities, making them more vulnerable to world price changes in that single commodity. They may also have greater import dependence, as their economy may not be of sufficient size to produce a great diversity of products. Regarding matters of geography, many small economies happen to face greater costs due to greater distance from large markets and from suppliers and many happen to be particularly vulnerable to natural disasters. They still have a comparative advantage in some products, but the absolute disadvantage means they can never secure a high income (Winters and Martins 2004: 348).

All this means that these small countries in free trade would possibly find that they cannot establish a commanding position in any export. They have relatively high costs due to inability to match the economies of scale of larger economies and the cost of importing inputs from distant regions as well as high transport costs in shipping their goods to large markets, which are also distant. Their unusually high reliance on imports for many essentials may make inhabitants particularly vulnerable to fluctuations in world prices and in export revenue (with which to pay for imports) in the absence of interventions to stabilise the effects of these on the economy.

7.3.1 The balance of various aims of the WTO implicit in its preferential treatment scheme

Let us pause and recall the aims of the WTO. We noted that some of them may conflict in their proposals. Having seen some reasons for SDT, let us relate them to the aims. SDT measures violate the principle for reciprocity. The GSP (Generalised System of Preferences) allows developed countries to make concessions to developing country exporters without an expectation of reciprocal concession. The sidelining of the developing countries in early rounds of GATT likewise allowed developing countries to benefit from MFN reductions in barriers without having to concede reciprocally.

SDT violates non-discrimination, allowing the developed countries to reduce barriers to developing countries without doing likewise for fellow developed countries.

The preferential treatment is arguably not mutually advantageous. It allows developing countries to undertake protectionist policy for reasons of infant industry protection but does not allow developed countries to do this for the same reason. Possible consequences of this are that producers in developed countries may face a fall in effective demand and in revenue. If the world market is dominated by a very small number of developed country firms and is thus far from the ideal of perfect competition, then the entry into the market of the protected or promoted producer *in the long run* may improve competitiveness. The foreign producers would then expect a fall in market share and in the super-profits which accompany monopolistic production.

The goal of optimal use of world resources suggests matters of productive efficiency. If countries in free trade specialized towards their respective areas of comparative advantage, we might expect factors of production in each country to be used in the production of the commodity where it has greatest use. The existence of trade barriers *may* hinder that. The extent to which it hinders this depends partly on how closely the ideal of perfect competition is approximated within a country and whether free trade between two countries moves both countries closer to, or further from, perfect competition.

The preferential treatment of developing countries is motivated by the reasons we saw in the previous section. The reasons relate to aims of the WTO that acknowledge the particular needs of developing countries and the possibility that preferential policy may be required to meet those needs. For example, the Preamble of the Marrakesh agreement states an intention by the contracting parties to raise standards of living and to secure full employment generally and for positive efforts to ensure that developing countries, and especially the least developed, secure a share in the growth in international trade commensurate with the needs of their economic development.

It is a matter of political negotiation, empirical assessment and practical reasoning as to what the *needs* of development of the developing countries are, and whether preferential policies would better allow them to raise the standards of living of their inhabitants and to reduce unemployment. The articles relating to preferential treatment suggest that export revenue and diversification may be an important means to meeting the needs of developing countries (whatever these are judged to be). Greater income from exports, as well as more stable income due to diversification, can be used to alleviate domestic poverty. Developing countries can also reap other benefits of development, such as having better infrastructure (which may be built by, or to accommodate, export businesses and may not have been built otherwise) and greater access to a range of technologies and know-how.

The articles relating to preferential treatment (some of which are mentioned above) also suggest that ways to help developing countries expand and diversify their economies include tools such as preferential treatment including infant industry protection and subsidies.

I will return to these matters when I compare the alternative proposal elaborated below with the existing WTO scheme. In the meantime, let me mention some criticisms of the existing SDT arrangements.

7.4 Criticisms of existing arrangements for SDT

Both debate internal to the WTO and academic literature external to it contain various criticisms of existing SDT measures. The criticisms are used to different ends by different authors, and there are many proposals for improving the system: for example, fine-tuning the SDT provisions; changing the sorts of industries in which SDT provisions have had most impact; reducing the role of some sorts of SDT in trade negotiations; and alternative systems of preferential or progressive trade regulations. I will use the criticisms as basis for a particular alternative, namely, the Market Access Proposal discussed below. For now, let me list some of the criticisms in the literature. For ease of presentation, I group the criticisms under three loose sub-headings: costs imposed by the SDT scheme on developing countries; bias against the areas of greatest interest to developing countries; and unnecessarily moving trade further from efficient specialisation.

Costs imposed by the SDT scheme on developing countries

Rules of origin are regulations determining a product's country of origin. An importing country can sometimes impose different tariffs or duties on imports from different countries, perhaps because of differential treatment of particular groups of developing countries or because of bilateral trade agreements. Determination of country of origin affects the tariff or duty that is imposed. There are currently many bilateral trade agreements and preferential treatment arrangements. Rules for determining country of origin and tariff rates vary from country to country. Often products contain components or inputs from many different countries. All of this combines to make determination of country of origin a complex matter which imposes transaction costs on exporters. The cost lies in researching and assessing the likely duties one must pay to export to a given country and in keeping up with the countries of origin of all components. This is particularly costly for small corporations and traders, and for developing countries (Sutherland et al 2005: 22).

Policy makers and advisors have finite resources and must make trade offs. Keeping up with the complex negotiations on SDT at the WTO and on GSP with particular developed countries can require a lot of resources. Yet, greater preferential market access in international trade is only one aspect of poverty alleviation and accordingly, there is an opportunity cost to this use of resources. For, there are other critical areas in poverty alleviation such as macro-economic policy, basic health provision, infrastructure provision, education, effective governance and property rights. There is the danger that the Doha Development Agenda of the WTO (part of the most recent round of WTO talks) and, more generally, negotiations regarding preferential market access through GSP and SDT, can absorb all trade-policy making resources and much bureaucratic and analytical capacity in many developing countries, at the expense of other development areas (Winters 2002: 1-2). If preferential treatment is desired, an arrangement which avoided the complexity of the existing arrangements would be preferable insofar as it would free up more scarce resources for other urgent needs in developing countries.

The *utilization rate* is the ratio between imports covered by a GSP scheme that actually receive preferences and imports covered by a GSP scheme. There are many reasons why, even though a product is covered by the GSP scheme of a country, its developing world trade partners do not export that product to it in large quantities. For example, there may be high compliance costs, restrictive rules of origin and a lack of understanding of technicalities. The low level of industrialization and diversification

in many developing countries may mean that they are unable to initiate or expand production of many of the commodities covered by a GSP scheme (Page and Kleen 2005: 14-5). It may also be because of ongoing uncertainty about tariffs in the future. To function as an incentive to traders in developing countries, preferences must be predictable and stable enough to allow traders to rely on them in planning exports and increases in production. For various such reasons, the utilization rates for developing countries are generally quite low, especially for LDCs (UNCTAD 1999: para 56-7).

Bias against the areas of greatest interest to developing countries

There is a lower preference margin on agricultural goods than on industrial goods. (Recall that the preference margin is the difference between the tariffs set on imports from the preferred developing countries and the MFN rate (the tariffs set for other, non-preferred, countries)). It is generally granted that the poorer developing countries depend more substantially on agriculture and the primary sector more broadly. The comparative advantage of developing countries generally lies in the primary sector. The fact that preference margins in this area are nonetheless lower, may reflect the fact that *grantor* and not *grantee* interests determine the preferences (UNCTAD 1999: para 53).

The Enabling Clause does not place formal obligations on developed countries²⁶. The exemptions from MFN, for example, are entirely voluntary on the part of the grantor developed countries. The grantors are not obliged to give tariff preferences at all, and in cases where they do choose to provide tariffs, they decide unilaterally which products and countries will be covered.

Once preferences are granted, they are not binding on the grantor countries and can be altered to exclude certain products, or even withdrawn entirely at the grantor's discretion. Without binding obligations, preference providers face pressure from their own import-competing domestic lobbies to minimise the scope of their preferential schemes. The result is that interests in the preference grantor country, rather than the interests of the grantee country, determine the products covered and the types of preference offered.

In the case of the EU's GSP (Generalized System of Preferences), once the scheme led to successful exports, the EU began setting annual quotas that considerably restricted the advantage that the exporting countries could extract from the preferences. Or again, in 1992 US withdrew \$60 million worth of pharmaceutical imports from their preference scheme because the US Trade Representative determined that India had weak patent protection that adversely affected US companies (Sutherland et al. 2005: 25).

Unnecessarily moving trade further from efficient specialisation

I have mentioned that differential treatment in terms of tariff rates creates a 'preference margin': the difference between the rate imposed on all other countries (the MFN rate) and the rate imposed on the preferred country. The margin allows the preferred country a competitive edge over other exporters. The preferred country develops an interest in stalling negotiations to reduce MFN rates, because such a

²⁶ For a discussion of the feature of SDT provisions that they are not legally enforceable, see Keck and Low 2006 pp153-4.

reduction would narrow the preference margin and thus its competitive edge (Sutherland et al 2005: 23). Since some developing countries face the MFN rate while others face the preferred rate, the latter countries' stalling of negotiations to reduce MFN rates hurts the former developing countries²⁷.

Insofar as the preferences apply to one group of developing countries and not to other developing countries, they often simply *divert* trade from some poor countries to others, at the whim of the country granting them. That is, while a country may have been importing from developing country X before preferences, after preferences, it finds it cheaper to import from developing country Y. In terms of efficiency, trade diversion can switch demand away from an efficient (but not-preferred) producer to a less efficient (but preferred) producer.

The EU's 'Everything But Arms' (EBA) agreement granted duty free and quota free access for all LDC (Least Developed Countries) exports except for arms and for three sensitive agricultural products. To put this preference into context however, note that the LDCs produce almost nothing that is directly competitive with EU production. The countries produce such small amounts that the removal of duties on their exports will rarely reduce prices sufficiently in the EU to expand demand from EU consumers. Instead, the EBA diverts EU purchases from other countries to LDCs. Generally the countries which compete most closely with the LDCs are countries whose incomes fall just outside the 'least developed' limit. These countries, very nearly as poor as the LDCs, see their demand diverted to LDCs (Winters 2002: 25).

This does not benefit the developing world as a whole, but only shifts the same amount of export revenue from one needy country to another. Moreover, since the choice of preference recipient is up to the grantor country, this leaves some potential for political favouritism and punishment in extending or withdrawing preferences to developing countries (Stiglitz and Charlton 2005: 100).

A preferable system would institute a rule-based and principled mechanism for differentiating between rich and poor, and strong and vulnerable economies. Many possible systems can be designed with this aim in mind. I will investigate one proposal in the literature.

7.5 The Market Access Proposal

I will investigate and endorse an alternative system for greater market access for developing countries. Note that I am concerned only with greater market access and will not consider aspects of SDT which do not concern market access. For example, some SDT provisions are for technical assistance.

Further, it is a relatively bare bones account which needs to be supplemented with more specific measures to address problems of implementation. Nonetheless, the proposal is worth considering. In part this is because it answers many of the criticisms above. Moreover, it also shows promise as a way to increase and secure the benefits to developing countries of the international trade system. As I discuss in a section below, this makes the proposal interesting to egalitarians investigating ways to alleviate global poverty.

²⁷ For a list of criticisms of the way in which the preferential market access component of SDT is currently implemented, see chapter 2 of the report by the WTO consultative board (Sutherland et al. 2005). In particular, see paragraphs 89-102.

Stiglitz and Charlton propose the following principle around which to base a system of preferential treatment²⁸. Each WTO member should commit to providing free market access in all goods to all developing countries poorer and smaller than themselves. So all developing countries would expect free access to all markets with (1) a larger GDP *and* (2) a larger GDP per capita. (1) is the way in which the phrase ‘larger economies’ is understood for the purposes of this principle and (2) is the way in which the phrase ‘richer economies’ is understood (Stiglitz and Charlton 2005: 94). While developing countries thus have access to the markets of larger and richer countries, they are not required to reciprocate by opening their economies to these latter economies. The authors title this proposal the Market Access Proposal or MAP.

Countries with larger GDP would correlate roughly with countries where bigger economies of scale and bigger industries generally are possible. Businesses with economies of scale and big businesses in general are more able to swamp competing producers in smaller economies, as the latter producers tend to be smaller. Richer countries are likely to correlate with economies which have access to superior production technology and which therefore have cost or quality advantages. Higher GDP per capita is an indicator of the adequacy of safety nets, of poverty and therefore of the seriousness of the cost of an industry being swamped and driven out of business by competing imports.

The progressive nature of the MAP lies in allowing smaller and poorer countries open access to the markets of the wealthier countries, while maintaining protections against competition from these latter countries. It requires the most liberalization from rich developed countries, significant liberalization (towards poorer developing countries but not towards richer countries) from middle-income countries and very little liberalization from the poorest and most vulnerable. It requires most liberalization from ‘the quad’ – Canada, EU, US, Japan. It requires the least from African Least Developed Countries or LDCs. The median ratio of market access rights to obligations in the MAP scheme is 303:1; that is, the median developing country receives free access to markets 303 times the size of the markets to which it must give free access (Stiglitz and Charlton 2005: 98). This allows firms in the poorer countries to grow using infant industry protection and to gradually carve out a larger share of the world market. Ideally, the poorer economies would thereby increase their income, diversify their production, improve their technological capacity, improve attendant infrastructure, and move up the value added chain²⁹.

There are other ways of effecting this progressive sort of market access. Stevens 2002, for example, proposes that SDT should be provided to countries based on objective criteria. Various criteria would be applied on an agreement by agreement basis and SDT being available to countries which meet conditions indicating their need for exception or assistance.

For instance, access to some types of SDT in agriculture should be based on measureable criteria relating to food security. Countries could qualify for special treatment if they have a per capita calorie intake below a certain level, a high share of agriculture in GDP and a high share of food imports to GDP. Per capita calorie intake is taken to be an indicator of vulnerability to food insecurity. The share of agriculture

²⁸ See Charlton 2005, and Stiglitz and Charlton 2005 chapter 6.

²⁹ For some brief comments about the desirability of *non*-reciprocal trade relations between developed and developing countries in light of recent regional trade agreements see (UNCTAD 2007: 57-8).

in GDP indicates the importance of agriculture in livelihoods. The ratio of food imports to GDP indicates import dependency regarding food.

In the MAP scheme, the sizes of GDP and of GDP per capita are comparatively blunt indicators of need. They correlate roughly with features like bigger economies of scale and bigger industries, access to superior production technology and thus cost or quality advantages, adequacy of safety nets and poverty. These features in turn indicate economies that are more vulnerable to adverse effects of trade liberalization.

Compared to the MAP proposal, Stevens' proposal has the advantage of closely matching the needs of specific countries to special treatment of specific sorts. The disadvantage of Stevens' approach is that it makes trade negotiations more complex and raises transactions costs. On an agreement by agreement basis countries must agree on measurable criteria and on eligibility cut offs. It is arguable that neither international consensus nor the necessary negotiating capacity currently exists for this ambitious and resource-intensive SDT system (Stiglitz and Charlton 2005: 101).

By contrast, MAP is simple to negotiate. It does away with the complex set of preferences under the GSP (Generalized System of Preferences). The arrangement binds developing and developed countries alike. The underlying principle is that all countries should participate in an enforceable system of preferential market access in which rights and obligations are distributed progressively according to objective criteria. Since objective criteria determine the preferential treatment, there is no need for complex and costly negotiations between groups of countries and particular developed countries as there is in the existing GSP scheme. Choice of an appropriate position on the continuum between low transactions costs and transparency on the one hand and tailor made proposals on the other, is a matter of negotiation by the contracting parties. However, I have chosen one option to investigate and have picked this option for the reasons of simplicity, transparency and low transaction costs.

7.5.1 Situating the MAP within WTO norms

This MAP would be binding on all members of the WTO. Under the proposal, developing countries have the *option* of providing key industries with some protection from competing countries that derive advantages from either the scale of their economies or from technological advantage. The smaller countries can, of course, choose to remove protections against imports from larger and richer economies. They may want to do so, if, for instance, they can thereby obtain some essential goods more cheaply than can be produced domestically.

The proposal involves significant liberalization. This is in keeping with the WTO's commitment to the aim of removal of trade barriers. In particular, the proposal involves significant liberalization of trade *between* developing countries. . Most Doha Round estimates indicate that the potential welfare gains for developing countries are larger from liberalization by other developing countries than from liberalization by developed ones³⁰. This is partly due to the fact that developing countries generally have higher tariff rates than do developed countries.

For many countries, the only option for reaching the minimum scale needed for sustained growth is to integrate with the greater world economy in order to access a larger market. The MAP allows this: developing countries have access to the

³⁰ See Francois, van Meijl and van Tongeren 2003

markets of richer and larger countries. Yet at the same time, it allows the countries to manage major import threats from the competition of these bigger economies who derive advantages from either the scale of their economies or from technological advantage (Stiglitz and Charlton 2005: 95-99).

Consider how the proposal fares with respect to some of the criticisms made of the existing SDT schemes.

MAP transforms discretionary and voluntary preferential schemes into well defined obligations within WTO. This has several advantages over existing SDT. As discussed in the criticisms, the discretionary and non-binding nature of current SDT provisions means that developing countries face uncertainty about whether granted preferences will remain in the future. This is one factor (among others) contributing to the fact that developing countries often do not take full advantage of greater market access due to preferences by expanding production in the relevant export areas. Firms are unwilling to make costly investments to initiate or expand production if they are uncertain whether they will retain in future the competitive edge they derive from preferences.

Since the greater market access is legally binding, developing countries have recourse through the WTO dispute settlement body to ensuring that trade partners fulfil their obligations.

Making such progressive market access *obligatory* means it is no longer grantor country interest and domestic business lobbies that determine the areas in which greater market access is granted. I discussed above how these interests mean that preference margins are far smaller on agricultural products (where developing countries have a comparative advantage) than on industrial products. Under MAP, barriers to *all* commodities from poorer and smaller economies will fall.

The existing scheme has much room for trade diversion. As we noted in the example of the EU, when preference margins are granted to some developing countries and not to others, the imports of the developed country often simply move from one trade partner to another. There may not be any change in the amount imported by the developed country and consequently no increase in aggregate export revenue for developing countries. As I noted, the penalty of diverting trade away from a country can be used as a tool of political manipulation of countries. Under MAP, barriers are removed for *all* economies smaller and poorer than one's own. Thus, a country reducing its barriers has no scope for treating this removal as a tool of political manipulation.

The MAP scheme is much more transparent than the SDT system. SDT negotiations are complex and absorb much bureaucratic and analytical capacity in smaller developing countries. Given that these resources are highly valuable and are scarce in many countries, the transparency of the alternative scheme is very welcome. With fewer negotiations and developments to keep up with, the bureaucratic and analytical resources are freed for other uses domestically.

Recall that under existing SDT provisions some developing countries resist reduction in MFN rates, as this would erode their preference margins (which are the MFN rate minus the preferential tariff rate). LDCs, for example, may lose out relative to middle income developing countries as the preference margins of the former diminish. With the MAP proposal, MFN liberalization by developed countries does not cause LDCs to lose out relative to middle income countries. A developed

country's MFN tariff rate applies to all economies larger and richer than it. Liberalization of the MFN rate affects the economies larger and richer than the liberalizing country. It does not affect those economies that are poorer than it is, as they continue to benefit from free access. Thus the MAP reduces the incentive for LDCs to block MFN reduction because of concerns about losing their preference margins (Stiglitz and Charlton 2005:99).

7.6 The MAP as a means to the egalitarian end of alleviating global poverty

It may seem that international trade should not prioritise the aim of poverty alleviation if it is not the instrument best suited to this. We may well wish to prioritise the aim of poverty alleviation over that of efficiency and optimal use of world resources. However, it may be that some other means such as foreign aid is the proper avenue by which to pursue the aim of poverty alleviation. In that case, it may be acceptable for rules of international trade to prioritise efficiency concerns instead.

However, foreign aid by itself is not likely to do the trick and needs to be complemented with changes in patterns of international trade. Trade has many potential positive effects beyond raising national income. I have just listed some of these benefits. Economic development through international trade also allows a sort of stability and certainty about a country's future. The contrasting instability lies in the fact that the fate of the country's poor rests to a large extent on the country's economic health. By comparison, a country reliant on foreign aid avoids having to rely on its own economic health, but is instead dependent on favourable currents in geo-politics so that its benefactors continue to donate large sums.

Moreover, note that much foreign aid would depend on developing country governments, as recipients of aid, undertaking infrastructural and other development for the benefit of domestic poor. By contrast, economic development and increases in national income which occur through international trade work to a large extent through private agents. Many infrastructural developments will occur purely through private entrepreneurship. Some of these will benefit the global poor. Jobs will be created and can increase income without depending on the government. I argue that reducing the reliance on government and raising the reliance on the market is preferable in this instance given the possibility of corruption and misuse of funds by governments.

Finally, the existing patterns of international trade are among the institutions which *determine* the distribution of income and wealth and the varying standards of living across countries. The MAP thus seeks to change the institutions which perpetuate or aggravate poverty and inequality rather than leaving those institutions alone and simply compensating for their effects through income transfers.

7.6.1 The MAP as a more egalitarian balance of developed country and developing country interests

I noted in section 7.3.1 that the existing SDT regime acknowledges that the aims of optimal use of world resources and the attendant focus on productive efficiency need to be balanced against the aims of helping the developing countries to develop, and to expand and diversify their economies. It is accepted on this basis, that some preferential treatment and some protectionism by developing countries is required in the foreseeable future.

The MAP might be thought to promote *greater* preferential treatment and to excuse developing country protectionism *more explicitly*. For, it makes the organizing principle a progressive one, explicitly jettisoning even formal or long term commitments to non-discrimination and reciprocity. The preferential treatment is not considered *exceptional* to an organising principle, but rather an instance of it.

In terms of the *stated* aims of the WTO agreements, this does not leap much further than the status quo. It continues to rest on the judgment that some preferential treatment and some protectionism by developing countries is required in the foreseeable future. It merely phrases this in the form of a new organising principle rather than as an exception to an organizing principle aiming at non-discriminatory and reciprocal removal of all trade restrictions.

Consider the distribution of costs and benefits from international trade across countries. Countries benefit to greater or lesser extents relative to one another. Given its progressive nature, the MAP is expected to benefit the developing countries relatively more than is the case under the status quo.

In the proposal, developing country firms will be better able to compete against established developed country firms on the world market. Reduction of developed country import barriers and export subsidies will make developing country exports more competitive on developed country markets. Developing country protections will allow fostering of infant industries and possible moves up the value-added chain.

From the Heckscher-Ohlin model (discussed in chapter 6), we can expect that factor incomes such as wages and returns to capital will move towards greater equality across trading partners. Some factor incomes in the developed countries will fall. Moreover, developed country producers that currently dominate particular markets may see their market share eroded. These are expected parts of increased competitive international trade but will likely be accelerated by the implementation of the proposal.

Consequently, it is likely that there will be a progressive redistribution of wealth from the developed countries to the developing countries. Low-skilled workers will bear the brunt of this loss in the developed countries. It is hoped that their governments will counter this with measures to improve the welfare of domestic poor. These measures may include improved domestic safety nets, more progressive domestic redistribution of income, improved access of the domestic poor to basic needs such as healthcare, education and shelter, and government initiatives to develop new industries and employment.

Despite this cost to the developed countries, this proposal is reasonable because of the benefit for the global poor, and the ability of developed country governments to mitigate the costs imposed on their domestic poor. Given the much greater wealth and better infrastructure of developed countries, their governments are in a better position to care for domestic poor than are the governments of developing countries to care for their own domestic poor.

All this begs the question: is it reasonable to suppose that the developed countries would want to be party to a system of rules for international trade designed according to the MAP? I argue that the answer is yes. If a system of distribution of advantages is considered to systematically take more from some and give more to others, this can nonetheless be acceptable. Consider the analogy of progressive

taxation of individuals in a society. Putting aside moral considerations, the rich accede to the tax system (as part of the greater governmental order) because they *do* get some benefits. The benefits include matters of order, legal recourse to pursue wrongs, definition of things like property and rights. Likewise, the rich countries might accede to a system of progressive international trade rules because the greater international order provides benefits of stable and certain tariff rates, a dispute settlement system, avoiding retaliatory tariff wars, lower prices for consumers in developed countries, and so on.

Parallels can be drawn between the aims of this progressive design of international trade rules and familiar progressive issues at the domestic level. These parallels may help make the proposal more palatable to those with progressive opinions in domestic policy. For example, this political decision parallels in some ways the politics of domestic progressive distribution of income where such domestic redistribution is thought to lead to losses in efficiency and to incur costs on the better off. Of course, there are also relevant differences. An obvious difference is that the proposal is not for income redistribution but for changes to background institutions (namely, rules of international trade) which partly determine income distribution.

Another parallel is affirmative action and equality of opportunity. As a point of economic history, most of the now developed countries - including Britain, the United States, Japan, Germany, and others – used protectionist trade policy and significant government intervention to develop their economies and raise national incomes. The same is true for the newly industrialised countries such as Taiwan and South Korea. Insofar as some of these countries advocate that developing countries remove all protectionist barriers, they can be seen as kicking away the ladder to the top after themselves having used the ladder (see Chang 2002 for the economic history). It might be thought that preferential treatment of the developing countries – allowing them to use some protectionist policies which the developed countries are denied – simply allows them to catch up and level the playing field. Just as affirmative action (unlike institutional racism) is not viewed as unfair, the proposed preferential treatment need not be viewed as unfair.

My intent in making these parallels is not to argue that *since* there are some similarities, we have similarly strong reasons for progressive policy nor, moreover, that the progressive policy in the global case ought to be of the sort I propose. Such an argument would first have to establish that the *dissimilarities* between the cases are not relevant to the political decisions. I do not make that case. Let me state explicitly that my reasons for advocating MAP over the status quo are the following egalitarian concerns.

The *absolute level of poverty* of the global poor is appalling - a sentiment familiar to the egalitarian intuition of ensuring no one is below a minimum threshold of basic goods. The *inequality in wealth and conditions of life* between the global poor and the global rich is enormous enough to warrant the judgment that the distribution of these advantages has not adequately prioritised the interests of the worst off – a sentiment relating to the egalitarian intuition captured by the priority view. As Pogge has powerfully argued, the global rich are *responsible for* the economic and political order which maintains and perpetuates this inequality and abject poverty. That is, that the global rich have not only positive duties, but also negative duties to help the global poor.

When compared to the status quo, the MAP appears promising as a way to increase the national incomes of the developing countries and to improve the infrastructural development of those countries. The proposal is likely to result in a progressive re-distribution of wealth in favour of the developing countries. It will create fairer institutions of international trade, allowing the developing countries to catch up to their developed world trade partners and competitors. The tendency of the institutions of international trade to perpetuate inequality and poverty is likely to lessen under MAP. Accordingly, the resulting institutions of international trade will be more just.

7.6.2 Likelihood of the MAP

The crucial question with respect to the MAP proposal is whether it is politically likely to eventuate. This question must be considered alongside other questions about the desirability of MAP in relation to other egalitarian reforms of the rules of international trade that may be politically more likely. This is an interesting area of egalitarian investigation, but is not one which I undertake. Let me make some brief points about some of the concerns that would figure in such an investigation. These points link back to section 5.1.3, where I mention some of the positions egalitarians oppose, and some of the ways in which egalitarians oppose others.

Some opponents to the MAP will say, at least in public, that they value development, but that the MAP is simply not the best way to achieve it. The egalitarian must assess the validity of the objection, comparing the proposal to others, taking care to determine likely costs and benefits. If the egalitarian emerges from this assessment committed to MAP, she must clarify the reasoning behind MAP (or other progressive policies which she finds preferable), and make the case that they lead to an improvement over the status quo.

The World Bank, the International Monetary Fund, the WTO, and developed country governments explicitly value the aim of alleviating global poverty, and of helping developing countries develop. Given this common ground, the merits of the MAP (or other progressive proposals found to be preferable upon greater egalitarian investigation) should be presented forcefully and effectively. Efforts to increase visibility of such ideas and proposals outside of policy circles – such as in academia, as well as in popular media – should occur to increase pressure on policy makers to respond to these issues. NGOs have been carrying out such campaigns on various issues of egalitarian concern. The Jubilee debt relief campaign and related campaigns have made the issue of sovereign debt highly visible in recent times. Joseph Stiglitz's books on fair trade and globalization, written to be accessible to non-academics, are a different sort of attempt to make these issues more visible. If opponents concur with the general aim, but object that the costs to them are too great, then there should be negotiation to come up with an acceptable compromise.

Others will be unwilling to bear any substantial cost, no matter how much it benefits the global poor, and no matter if it is judged to be the best way to benefit them. These individuals are likely to see the costs as too great in terms of loss of wealth, comfort, lifestyle, geo-political power, reputation, and so on. These individuals are likely to have the greatest influence over the levers of power. At the very least, an effective and public egalitarian campaign can make it embarrassing for the relevant policy makers to reject the proposal. For, the policy makers may be forced to abandon public pretence to altruism. More substantially, egalitarians should seek means of convincing these opponents.

One general approach would be to seek threats that the beneficiaries of the MAP proposal could make to change the perceived balance of costs and benefits on the part of the opponents. This would be akin to the use of strikes to gain worker rights and other progressive concessions from opponents who controlled the relevant levers of power. Some, such as George Monbiot, have floated the possibility that developing countries can band together and threaten to collectively default on their sovereign debt in order to extract progressive change from the developed countries (Monbiot 2003: ch 5) such a possibility must be investigated. Relevant considerations include the following. It must be assessed whether the parties who would stand to lose significantly from the debt default coincide with, or have sufficient influence over, the opponents to the MAP. It must be assessed whether enough of the developing countries with large debts would be willing to cooperate on this initiative given the potential costs of worsening relations with the developed country governments. It must also be assessed whether such a threat would be credible to the developed countries, given that the threatening countries risk losing access to creditors in the future and may see the risk as too great to follow through on the threat.

In this chapter, I have described the ways in which the rules set by the WTO can be changed to allow preferential treatment for developing countries. I described existing special and differential treatment of developing countries and presented various criticisms. Then I presented the Market Access Proposal as a way to allow even more preferential treatment of the developing countries with the aim of helping them raise national incomes and develop their economies. I presented the proposal as a means of global wealth redistribution and poverty alleviation. The proposal attests to the fact that technically feasible means exist that can contribute significantly to global poverty alleviation and that only await a political decision to be implemented. I advocate the proposal from an egalitarian perspective as it seems likely to further egalitarian aims. Whether it is the proposal most worthy of egalitarian political effort and advocacy, is to be judged in a broader egalitarian investigation which examines other possible reforms for egalitarian ends.

In the next chapter, I turn to an investigation of some issues surrounding sovereign debt.

Chapter 8: Sovereign Debt

I take it for granted that the reader shares an understanding of the burden of debt service for the poorest countries. I only present a few indicative figures. The total external debt of the 'low income countries' (that is, those which have an annual average income of less than \$875 per person) was US \$379 billion in 2005. During 2005, these countries paid nearly \$43 billion to the creditor countries in debt service. For all developing countries in general, total external debt owed in 2005 was \$2.7 trillion, and over the course of that year they paid \$513 billion servicing these debts (Jubilee debt campaign website).

Third world debt has risen from approximately US\$70 billion in 1970, to \$540 billion in 1980 to \$1.34 trillion in 1990, to \$2.28 trillion in 2000 and \$2.6 trillion in 2004 (of which \$1.6 trillion is public debt). The indebted developing countries have repaid roughly US\$5.3 trillion in debt service (principal and interest) between 1980 and 2004. About 38% of the budgets of African states are devoted to debt service. Cameroon spends 36% of its budget on debt service and 4% on social services. Zambia spends 40% and 6.7% respectively; Nicaragua spends 14.1% and 9.2% respectively (CADTM 2005).

An investigation of sovereign debt of the developing countries is of interest to the egalitarian for the following reasons. Debt service for heavily indebted countries can divert scarce resources away from domestic poverty alleviation programs. This is a concern because of the absolute level of poverty of the poor segments of the affected populations. The institutions surrounding sovereign debt are unfair, and do not place adequate emphasis on debtor interests. Some of the debt is odious. Some of the debt management institutions allow external agents control over important parts of a country's domestic economic policy. This is a sort of domination of the country by external sources.

An egalitarian investigation of sovereign debt highlights certain facts. The burden of debt service is crippling for many developing countries and is large for many more. The opportunity cost of debt service in many cases is decreased government spending on poverty alleviation initiatives including health and education expenditure. More generally, the opportunity cost is likely to be less domestic investment and slower growth. Yet, economic growth is a strong potential contributor to poverty alleviation. This is a concern for the level of *abject poverty* of the global poor affected by sovereign debt.

The credit market for sovereign debt is unfair in that it encourages over-lending. The burden for this is borne ultimately by the residents of debtor countries, especially by the poorer sections of the population. Meanwhile, the benefits from the arrangement accrue primarily to lenders in the developed world. Employees who broker deals for private credit companies are rewarded for having brokered large loans. Shareholders in these lending companies benefit because the increasing loans are serviced on time (through yet more loans). This is a concern about fairness, as well as about the fact that the interests of the global poor are not being given adequate priority. These features of the sovereign debt arrangement systematically benefit individuals among the global rich, and the large cost is heaped on the global poor. There is unfairness in the existence of *odious debts*, where residents of indebted

countries are held accountable for loans undertaken by undemocratic rulers who may well have repressed sections of the population and diverted the loan to private coffers. The beneficiaries are corrupt and undemocratic rulers.

In the case of multilateral debt, the Bretton-Woods institutions, the World Bank and the IMF (unlike private creditors), impose *conditionalities* in exchange for loans. The conditionalities allow the institutions some control over the economic and social policies of the debtor countries. One reason this is a worry is because of the possibility that the lenders can use this influence over policy for their own interests. While the lenders are multilateral, their decision-making bodies and mechanisms are heavily dominated by and biased towards developed world representatives, in particular the US. This is a concern relating to the *domination* of domestic decision-making institutions and politics in poor countries by the multilateral lenders³¹.

I propose various remedies below, picking up ideas from the existing literature on sovereign debt. Some concern immediate debt reduction. Others concern the design of new institutions to slow the accumulation of debt in the future and to rectify the unfairness of existing institutions. The proposals tackle different aspects of the sovereign debt issue, and are intended as complementary changes rather than as substitutes. With respect to highly indebted countries, and countries with odious debt, I propose *debt reduction*. I also present possible measures to reduce the chances of *future accumulation of odious debt*. These proposals apply to certain groups of countries and not to all debtor countries. I also consider some proposals which are relevant to all debtor countries. In particular, I consider some institutional reforms in relation to private external debt, and outline plans for a sovereign bankruptcy mechanism to allow countries to manage problems in servicing public debt³². The latter mechanism is intended to improve the balance between debtor and creditor interests in the credit market and thus create a *fairer institution*.

The debt reductions immediately relieve the burden of debt on the heavily indebted countries and release more government revenue for poverty alleviation projects. The new institutions proposed in relation to odious debt reduce the possibility of accumulation of odious debt in the future. The reforms proposed to external private debt will serve to ensure that private debt remains private, so that governments are not required to rescue private borrowers and thereby increase the public debt burden placed on tax payers. The proposed creation of a sovereign debt mechanism would allow debtor countries to manage their debts better, reducing payment or easing terms of payment in case the payment cannot be afforded without strain on poverty alleviation programs.

In section 8.1, I describe the main agents involved in the sovereign debt institutions and outline some preliminary basics of credit markets. This is necessary

³¹ For a Luck Egalitarian/Liberal Egalitarian look at some aspects of sovereign debt see Cappelen, Hagen and Tungodden 2008. They discuss how the Highly Indebted Poor Countries initiative fares according to liberal equality principles *per se* (while acknowledging that a fuller assessment of HIPC must look at other moral criteria as well).

³² For a couple of other promising ideas, see (Stiglitz 2006: 236-7). Stiglitz suggests that lending should be denominated in the debtor's currency and that the international financial institutions should return to *counter-cyclical* lending. If lending thus occurs at times of troughs rather than peaks in a country's business cycles, this helps the country smooth social spending.

context for the discussion to follow. In section 8.2, I present some recent history of sovereign debt, in order to outline some of the main reasons for the accumulation of such a large debt by many developing countries. I emphasise as contributing causes certain institutional features of sovereign borrowing, as well as the actions of particular collective agents such as creditor governments, and the Bretton Woods institutions (the IMF and the World Bank, henceforth referred to as the BW institutions). These motivate some of the institutional changes prescribed in section 8.5. In section 8.3, I describe some liabilities of lenders, connecting to the actions of lenders mentioned in 8.2. This also connects to the proposed reforms in section 8.5. In section 8.4, I describe and criticise the Highly Indebted Poor Countries (HIPC) initiative which has been instituted recently to offer some debt relief to a group of poor countries. These criticisms motivate the recommendations regarding debt relief for heavily indebted countries in section 8.5.1. In section 8.5, I consider some possible reforms of the existing institutions.

8.1 Basics of the credit market

8.1.1 Types of lenders and of loans in sovereign borrowing

The external debt burden of a country is the money owed by private debtors (companies) and by the government to foreign creditors. Roughly 62% of external debt in 2004 was owed publicly and 38% owed privately (CADTM 2005). There are various reasons why a government will borrow. We will focus on particular reasons for borrowing which are most relevant to sovereign debt crises. One reason is if export revenue is insufficient to buy all the required or desired imports. This shortfall can be covered by national reserves, but, failing that, a loan may be sought. Another is for large government investments such as in building essential infrastructure. Yet another is in order to repay other debt.

Governments may be debtors indirectly. For instance, they may be a guarantor for a public or private enterprise that directly undertakes the loan. As guarantor, the government affirms that they will pick up the tab in case the borrower defaults. This is done because governments are usually seen as less risky than other borrowers and this may lower the interest rate at which the loan is given. These are *contingent* liabilities for the government – it may be liable *if* the direct debtor defaults on debt.

A debt crisis occurs when the usual creditors lose confidence in the ability of the sovereign to repay and therefore are unwilling to continue lending.

The main types of lenders to sovereign borrowers are commercial banks; multilateral institutions such as the IMF, the World Bank and various regional development banks like the Asian Development Bank, the African Development Bank, and the Inter-American Development Bank; official loans from governments (bilateral loans), generally developed country ones; and lastly, ordinary bond holders who buy on the market.

Bilateral debt is generally of two sorts – ‘aid debt’ and export credits. Aid debt consists of loans given to finance infrastructure projects and other development works. With export credits, which constitute the bulk of bilateral debt, the debtor country imports goods or services from the companies in the creditor country. For example, the debtor country may ask a foreign company to undertake some

construction work. If the debtor country cannot pay the company at the conclusion of the construction, the creditor government pays the company. The creditor government pays this amount as a loan to the debtor country and expects repayment. The export credit is the guarantee by the creditor government to domestic export firms that ensures they will get paid if they export to the debtor.

The poorest countries often do not find private agents willing to lend to them. They borrow from multilateral and bilateral lenders, generally at concessional rates. Loans from governments include the Official Development Assistance (ODA) funds disbursed by the OECD group of developed countries via the Development Assistance Committee (DAC).

Many 'emerging markets' have begun issuing bonds as a substantial form of borrowing. Emerging markets include about 25 or so developing countries that are rapidly industrializing and that are commonly considered somewhat in-between developed and developing country status. The bonds are sold to ordinary investors on the market. The government borrows money through the bond, and agrees to repay it with interest upon maturity to the bond holder. The bond market trades in these bonds between buyers and sellers based on their assessments of what the bond is likely to fetch upon maturity. Commercial and investment banks often act as intermediaries in the issuing of bonds by emerging economies. They help structure the bond offering, market the initial issue and underwrite the issue as they effect their sale to first buyers (Herman 2008: 15).

All in all, roughly 22% of external debt in 2004 was owed to multilateral institutions, 20% to bilateral governments and 58% to private creditors (CADTM 2005).

8.1.2 Credit markets and risk

In the general operation of a credit market, the lender expects that, some of the time, a borrower will fall behind on payments or will default altogether, unable to repay the outstanding amount. This risk is a normal part of credit markets. Based on their assessment of the riskiness of a loan to a given client, creditors charge different levels of interest. They charge higher interest rates for riskier clients. If the loan is fully and unproblematically repaid, some of the higher interest collected can be set aside as a *loan loss reserve*. This reserve makes up for cases of default.

The existence of risk acts as an imperative on lenders to judge the creditworthiness of borrowers, and the likely success of the investment planned by the borrower. Insulation from existing risk leads to *moral hazard*: the private creditors, expecting that they are insulated from adverse consequences of risky lending, act less carefully than they otherwise would. In such cases, there will be over-lending.

One element contributing to the accumulation of developing world debt is that their creditors have been insulated from risk and have therefore over-lent. Before the advent of the Bretton Woods institutions, risk was allowed to play some role in sovereign borrowing. When sovereign states defaulted, their lenders often bore the cost. There were, of course, occasions of military action to recover debts forcibly, and these shielded creditors from risk. Yet at the same time, much money was simply lost. There were many default negotiations concluding in a debt reduction. Here are a few

examples of negotiated debt reductions and unilateral debt defaults. The British and French governments defaulted in the 1930s, saying that the welfare of their populations were more important than honouring the presumption to fulfil contracts in this instance. In the 1940s, nine US states suspended interest payments when their main export – cotton – could not fetch enough of a price. The 1953 London Accord halved Germany's foreign debt (Raffer 2007: 87-8).

In the 1970s however, creditor governments bailed out their banks even when they did not adequately take account of risk. Private creditors thus received the signal that they did not need to cautiously assess risks, be selective in lending, and be prepared to suffer losses and to plan accordingly. An illustrative example is the case of US banks' lending to Indonesia in the early 1970s. US government agencies warned private creditors about the bad state of existing Indonesian debt. The IMF placed a ceiling on the Indonesia's external borrowing. Yet, private creditors used technical tricks to get around these restrictions, and continued to lend. When the expected crisis developed and it seemed the creditors would be out of pocket, the US government indeed bailed them out (Raffer and Singer 2001: 162). Bail outs by creditor governments as well as by the multilateral institutions (see section 8.2) led to a climate of over-lending.

8.1.3 What is the usual recourse when there is inability to service a debt?

Countries generally have legal mechanisms for handling difficulties in servicing debts. These serve debtors who are individuals, corporations, or even sub-sovereign bodies such as a municipality. The mechanisms can include arbitrations between creditor and debtor to work out a restructuring of the loan – perhaps to change the term of the loan, or reduce interest, or postpone payment. Debt reductions are also possible. For corporations, there may be debt-equity swaps, where the creditor erases some debt in exchange for shares or control in the company. A loan can be refinanced by obtaining a new loan. Insolvency occurs for a person or an organization when financial assets are insufficient to cover financial liabilities. A debtor claiming insolvency can appeal to be legally declared bankrupt.

In general, law surrounding bankruptcy balances the principle of honouring the debt rightfully owed to creditors against the principle of ensuring that one must not be forced to fulfil contracts if that leads to inhumane distress. Such distress would include the seizure of basic means of sustenance for an individual, for example. If the debt cannot be met without causing inhumane distress, then some level of repayment less than full is negotiated through an arbitrator and both debtor and creditors are bound to it.

There are some special concerns when the agent seeking bankruptcy is a governing body. The US Code, for example, deals with such agents separately in chapter 9 of its title on bankruptcy. What are commonly referred to as 'chapter 9 proceedings' allow for the adjustment of debts of a 'municipality' (essentially, a sub-sovereign body within the state, such as a city or a county). Given that the financial future of the municipality will affect the lives of its residents, those who have a right to be heard during a hearing on a possible bankruptcy, include municipal employees, local residents and non-resident owners of real property among others (US Code title

11 ch 9). This allows an avenue for residents to voice their concern if they would be caused great distress by possible actions taken against the municipality.

Certain revenues and assets of the municipality are immune to seizure for the sake of repaying debts. These are to do with basic services that a municipality is expected to provide for its residents, such as transportation or utilities (11USC 902, 927). This is one avenue whereby inhumane distress to residents is proscribed.

Moreover, unless the debtor municipality consents to this, the court may not interfere with the political or governmental powers of the debtor, or with its property or its use or enjoyment of any income-producing property (11USC 904). This is to respect the value of sovereignty. Unlike other debtors such as corporations, municipalities are representatives of citizens and their means of self-government. This value of municipalities to their citizens remains protected.

There is no international legal mechanism for dealing with insolvency of sovereign states. This absence is another prominent factor contributing to the large debt burden of developing countries.

8.2 Why are so many developing countries in such substantial debt?

There are some specific historical factors behind the large debt of developing countries today. Let me note some of these.

Several factors in the 1970s contributed to a substantial rise in sovereign debts owed by developing countries. Non-oil producing developing countries experienced a rising overall trade deficit. The largest share of this deficit was due to a deficit in trade with the industrialized countries. A smaller, but nonetheless important, share was due to the rise in oil prices (GATT 1980: 8ff). Moreover, interest rates were relatively low, making it cheap to borrow. Loans were used to finance the deficit.

At the start of the 1980s, interest rates shot up. Many of the major industrial countries were running budget deficits at the time, and were consequently borrowers. This pushed up the interest rates (World Bank 1985: 5). Previously negative real interest rates turned into historically high positive rates. Since a large share of sovereign debt was at variable interest rates, the burden of debt service rose substantially (Raffer and Singer 2001: 160).

Yet the developing countries could not service the greater debt burden by running consistent trade surpluses. For, they faced substantial protectionism by the major export markets, the developed countries (World Bank 1985: 6). They turned to new loans to finance existing debt payments.

8.2.1 Bail-outs and insulation from risk

Commercial banks regularly monitor sustainability of clients' borrowing. They carry out risk management to ensure the overall portfolio of loans extended is not too risky. Supervisory authorities regulating commercial banks also have a brief to monitor their portfolios for the same reason. Banks are regulated because they tend to undertake excessive risk at the prospect of profit. Riskier clients are charged higher

interest and are therefore more lucrative, as long as the debt is ultimately serviced. Management may discount warnings from risk managers especially as most banks are corporations with shares on the stock market and whose management is paid according to stock price movements which usually reflects short term profit performance and may place insufficient emphasis on long term viability of the portfolio (Herman 2008: 11).

Prudent conduct would see private creditors put aside part of the higher interest rate charged to riskier clients in a loan loss reserve. This reserve would compensate for cases in which the debtor is unable to repay a loan. Indeed this is part of the reason for charging higher interest in riskier loans – it allows compensation for the cases in which the risk does not pan out for the lender.

Risk insulation and over-lending have played a role in the history of developing country debt accumulation. While European banks generally maintained loan loss reserves with respect to sovereign debt, US and Japanese banks generally did not. In part this may be because of the different incentives attached to reserves in the different countries. Loan loss reserves are tax deductible for European banks, while US banks pay tax even on these (Raffer 2007: 91).

This propensity towards greater risk taking was not curbed by the big creditor governments. As we have noted, they bailed out banks. One reason for the bail outs may be that governments felt that the absence of loan loss reserves would make debtor defaults particularly painful for banks and that this justified mitigating the damage. Other reasons may be geo-political motives, and political lobbying of government decision makers by financial interests.

It was believed in 1983 that US lawmakers might require banks to refund excessive fees collected from Latin American countries. The banks charged high fees under the justification that there was a high risk that the countries might default. If they nonetheless did not really expect default – if they expected bail outs, based on previous government action – then they gouged prices (Raffer and Singer 2001: 163).

The final major factor contributing to the large debts of many developing countries occurred during the 1980s debt crisis.

8.2.2 Illiquidity and insolvency

Poland defaulted in 1981. Mexico declared itself unable to honour its debts in 1982. This marked the beginning of the debt crisis of the 1980s. Many countries were unable to service their debts and defaults threatened and occasionally occurred.

For most of the 80s, the overriding perception among the Bretton Woods institutions and the creditor governments was that these debt problems were a sign only of *illiquidity* and not *insolvency*. The problem was taken to be the effect of a *temporary* inability to pay, i.e. illiquidity. The temporary illiquidity would be resolved as debtors experience greater economic growth and export revenues. Debtors were expected to grow their way out of debt in the long run. In this view, debtors simply needed to be supported in the interim period and did not need debt forgiveness.

The support in the interim period took the form of additional loans to restore short term liquidity. If a country had trouble making an interest payment, it found

ready access to another loan to allow it to do so. The new loans came from commercial banks as well as from multilateral institutions. A large group of commercial banks would form a syndicate and would, together, lend to a borrowing country. With debt servicing problems in the 1980s, many of the banks in the syndicates wanted to stop lending. These banks had perhaps only wanted to loan for a given period and did not want to make further loans to pay for the servicing of existing loans. Some of these banks left the syndicates, selling their claims to others on a secondary market. Others were convinced to keep lending by those syndicate members who did not mind a longer term engagement with the debtor country so long as payment eventually occurred. This ‘concerted’ or ‘forced’ lending thus kept the loans performing³³. That is, when a debtor country was in arrears, the lenders made new loans to clear these arrears so that, at least on paper, the loans were being repaid on schedule. The WB noted in 1988 that concerted lending from 1982 onwards had mostly been to clear the substantial arrears on interest payments rather than forward looking loans for productive investment (World Bank 1988: xxiv).

Moreover, during this time, multilateral institutions were becoming increasingly important as creditors. While concerted lending by commercial banks played its part in the refinancing of interest payments to ward off temporary illiquidity, the bulk of the refinancing was done by the multilateral institutions. By 1988, the WB was the principal net lender to the group of countries known as the heavily indebted countries (World Bank 1988: xxix).

This was, in effect, a bail-out. Commercial banks (like any lender in a well functioning credit market) had taken the risk that their loans might not be repaid or repayment may be delayed. When that possibility eventuated, they were effectively relieved of the burden of the risk as the multilateral institutions made new loans to ensure continued repayment. The multilateral institutions assumed the risk by bailing out the private creditors. Meanwhile, the cost of this for the debtors was substantial. Between 1982 and 1989, long term debt of all developing countries roughly doubled. The refinancing of loans relieved immediate liquidity problems, but it did so by increasing the present values of debt (Raffer and Singer 2001: 172).

What is worse for debtor countries is that, until recently, the BW institutions were less willing than private banks to reduce or reschedule claims. To maintain the image that the multilaterals do not reschedule loans, at times, the WB would lend to enable a debtor to meet the repayment deadline to the IMF, thus freeing up the IMF to lend to the country again to meet the WB’s repayment deadline. OECD governments also acted as intermediary financiers on occasion (Raffer and Singer 2001: 169).

Contrast how the countries would have fared if their situation were judged to be one of *insolvency* rather than of illiquidity. It would have been clear that the refinancing of loans would only raise the debt burden higher.

Countries which cannot service their debts and who do not want to undertake new loans can sometimes force creditors to the negotiating table. Argentina, for example, did so in 2002 when it realised that continuing debt repayment meant

³³ For more on concerted lending and its place within the history of sovereign lending over the past few decades, see, for example, (Herman 2008: 12-4)

tremendous sacrifice for its populace. It announced that it was unable to meet its debt obligations. It then negotiated with its creditors to convince them that it was preferable to receive some repayment rather than none at all. In 2005, 76% of its creditors settled for a repayment of approximately 34 cents on the dollar. However, Argentina prevailed only with immense negotiating skills and resolve and also faced considerable cost in that investors are put off investing in an economy in limbo, as was the case with the Argentinean economy in the years it took to reach a settlement. Most developing countries do not have the negotiating skill or resolve and may not be able to bear the cost (Stiglitz 2006: 215).

The existence of an adequate sovereign bankruptcy mechanism would make the process orderly and swift. It would also make this an option accessible to all developing countries. In the absence of a legal framework for sovereign bankruptcy, debtors may fear that declaring themselves insolvent or defaulting will drastically narrow options for future loans. The fear is that the debtor must maintain the perception of being credit-worthy in the eyes of potential lenders and that this perception may be damaged by default.

8.3 Legal and ethical liabilities of creditors

In well-functioning credit markets, creditors also have legal liabilities. Borrowers have a right to compensation if the lender was negligent in some respect and if this led to unlawful damage. This is part of the balance of rights and obligations legally distributed over creditors and debtors.

There is no adequate international legal mechanism governing sovereign borrowing. Accordingly, if a sovereign country feels wronged, it has no means of seeking redress against foreign creditors.

A discussion of liabilities in this political philosophical context must distinguish between two sorts of issues. One relates to negligence of the creditor *qua lender* in issuing the loan. Another relates to a broader sense of liability concerning the culpability of creditor governments and the BW institutions not *qua lenders*, but rather *qua political agents* who can shape the options available to debtor countries in borrowing and servicing. The protectionism of developed countries in areas of competitive advantage of exporting developing countries shows some degree of culpability of the developed countries in the large and growing debt burden of the developing. This is not a liability *qua lender*, but rather *qua political agent* more broadly.

There are links between these two in cases where the liability involves a bilateral or multilateral lender taking objectionable actions *qua political agent* which should arguably have led it to different actions *qua lender*. For instance, it may be argued that the bilateral creditors should have realised that their own trade protections made it hard for debtors to increase export revenue in order to service their debts. Accordingly, it might be argued that the creditors should not have treated debt problems of the 1980s as a matter of illiquidity and simply lent greater amounts *at least unless they were also willing to reduce their trade protections*.

Both bilateral and multilateral creditors have bailed out private creditors and have done so at the expense of large increases in the debt burden of the debtor country

in trouble. It can be argued that they should have noted the signals this sent to lenders about being careless in risk assessment and that they should have expected this could result in over-lending. They can also reasonably be faulted for not giving more weight to the possibility that the debt problems in the 1980s were indicative of insolvency rather than temporary illiquidity. Accordingly, they should have allowed the worst affected countries to default or to negotiate reductions rather than offering new loans to them.

The possibility that the countries with debt problems were potentially insolvent and not merely illiquid has been voiced by many over the decades, especially given that the indebted countries had dim prospects of enjoying substantial export surpluses and national income in the existing economic situation. Abbott (1972) notes that in the 1960s, many countries in sub-Saharan Africa were accumulating debt faster than their economies or foreign exchange earnings were growing (Abbott cited in Raffer and Singer 2001: 163). Pearson et al. 1969 (a report prepared at the request of the World Bank) had strongly recommended debt relief while a debtor experienced balance of payments difficulty (cited in Raffer and Singer 2001: 158).

Consider the prospects for growth in export revenue, and in national income, that the developing world overall faced in the 1980s and onwards. The existence of certain factors significantly reduced these prospects. One, greater export revenue and income would depend substantially on access to the large export markets of the industrialised countries. Yet, as we have noted in passing, there was significant protection of these markets in the sectors most relevant for developing countries (World Bank 1985: 6). Two, expansion of export industries in developing countries required investment capital which, for most of these countries, would have to be sourced overseas. Yet, as we noted above, soon after start of the debt crisis of the 1980s – and certainly by 1988 – new lending to sovereign debtors had mostly been to clear the substantial arrears on interest payments rather than forward looking loans for productive investment (World Bank 1988: xxiv).

There is a second distinction between two senses in which we can discuss liabilities. One is as a legal term, the other an ethical judgment. Legally, the absence of an international legal mechanism or international agreement on sovereign debt establishing rights and obligations of both lenders and creditors makes the issue of liability difficult. If legal redress is sought for alleged liability such as negligence of lender, it is unclear how successfully this could be done under domestic laws of creditor countries, using precedents for cases of loans not made to sovereign states. If an international mechanism for handling sovereign debt were to be constructed, it should make provisions for certain sorts of liabilities and protections relevant to the issues mentioned above. Surely, debtors will want to seek retroactive redress for loans which have already occurred. Whether the international mechanism allows for this is a matter of political negotiation between debtor and creditor governments in the design of the mechanism.

In terms of the first distinction, the legal notion of liability likely applies only to liability of a lender *qua lender*. It does not also apply to reprehensible action by bilateral and multilateral creditors *qua political agents* more generally.

An *ethical judgment of liability* may help build a case for a particular course of action in relation to debt reduction. Debate around cancellation of odious debt is the prominent example. The demand that the creditors bear the cost of being denied repayment is bolstered by ethical judgments of liability. Ethical considerations about liability for past actions may also figure in negotiations between creditor and debtor governments in the design and construction of a mechanism for handling sovereign debt. It can do this by, for instance, allowing poor debtor countries to extract more concessions from the creditor governments in defining the appropriate balance of creditor and debtor interests and protection.

In terms of the first distinction, ethical judgments of liability encompass both liability of lenders qua lender and also liability of official creditors qua political agents who shape the options available to debtors.

8.4 Debt relief programs for the Highly Indebted Poor Countries (HIPC)

The IMF and WB launched the Heavily Indebted Poor Countries initiative in 1996 to reduce the debt burden of bilateral and multilateral debt for some of the poorest and most heavily indebted countries. Forty one countries are eligible for debt relief under the program. Another program, the Multilateral Debt Relief Initiative, was launched in 2005 for a smaller subset of the HIPC countries. This promises further debt reductions for the selected countries. The aim of the program is to return the countries to a sustainable level of debt.

The HIPC initiative and related programs are certainly signs of progress and the BW institutions should be commended for changing the line they had held until 1995 – that the multilateral debt burden was not a problem (Raffer and Singer 2001: 183). Nonetheless, there are many criticisms of the program.

8.4.1 Criticisms of the HIPC initiative

Let me begin with some general criticisms before proceeding to criticisms specific to the way the HIPC initiative operates. The HIPC program is too limited in terms of eligible countries. There are many other countries with a large burden of debt diverting money from poverty alleviation programs³⁴. Many of them owe debts not only to bilateral and multilateral creditors – as the HIPCs *mostly* do – but also to private creditors. Even with the HIPC countries, some creditors – countries, banks and companies – choose not to take part and cannot be compelled to do so as the IMF and WB have no formal powers over them. An adequate sovereign bankruptcy mechanism with reasonable criteria for eligibility would allow many more countries to seek debt reduction and would encompass both official and private creditors.

Moreover, if countries could apply to an *independent* bankruptcy mechanism rather than to the creditors themselves under the HIPC initiative, we could expect that the terms would be more favourable for the debtors. It would remove potential conflicts of interest where the creditor is in charge of a debt renegotiation or relief

³⁴ A joint report by the NGOs Jubilee Debt Campaign, Action Aid and Christian Aid concludes that at least for 62 countries immediate and 100% debt cancellation is required in order to meet the Millennium Development Goals (Pearce 2005).

mechanism and could compel the BW institutions (and all other creditors) to accept responsibility for their part in creating or worsening the debt crisis.

8.4.1.1 Creditors setting the terms of eligibility and defining sustainable debt levels

Some criticisms of the HIPC program revolve around the fact that the creditors themselves – rather than a neutral third party – are in charge of various features. For example, the creditors determine the *eligibility criteria*, thus restricting the possibility of debt relief to a smaller number of debtors than is ideal. It should be expected – at least as a precautionary thought – that the creditor would want to minimise the sum of repayment foregone. There is an element of conflict of interests in the creditor setting the eligibility criteria. For example, the initiative focuses on a country's debt-to-export ratio as a criterion for eligibility. Yet this ratio has little connection to a government's ability to meet urgent social needs while servicing debts (Sachs et al 1999: 6). The criterion should instead be related to the amount available for government spending.

The part of a country's debt that is eligible for reduction makes a great difference to the impact of cancellation. At present, this is the amount of the debt at the time that a country entered a bilateral or multilateral debt relief program. However, the time taken over the debt reduction process from start to finish is several years. In the meantime, additional loans may be undertaken and compounded interest also functions to raise the debt. Impressive sounding commitments to cancel 90% of the debt of a country can be less impressive in reality if the percentage is calculated on the debt level of several years ago. In the years since its inception, only 23 countries have reached the 'completion point' where the overseeing institutions are satisfied that the debtor has and will follow the policy conditions. It is at this point that debt relief begins.

The concept of *sustainability* of debt is defined by the creditors and the threshold is set by them. At present, sustainability encompasses only financial matters – the level of debt a country can be expected to repay given estimates of its future economic growth. This definition ought to be changed so that sustainability is not merely financial but also social. It should encompass the ability to provide a decent level of social services and to invest in productive development (Sachs et al 1999: 4-5). Even for the purely financial calculation of debt sustainability, the cogency of the estimates of growth carried out by the IMF have been criticised for being too rosy. In effect, this raises the level of debt judged to be sustainable and lowers the debt reduction to which the creditors are committed (Donnelly 2007: 127) (GAO 2000: 51-3) (Stiglitz 2006: 239-40).

8.4.1.2 Debt relief is conditional on implementing certain economic policies

The HIPC and MDRI schemes require eligible countries to implement various economic policies as a *condition* for debt relief. I contend that debt relief should rest on the aim of lowering a debt acknowledged as having an unacceptable social cost. This implies no reason for the country to be forced to follow certain economic policies – other than perhaps transparency measures to ensure the money freed up from debt relief is used for social services and not funnelled into private coffers of the

rulers. A country's economic policy should ideally be determined democratically by its citizens. While the BW institutions are multilateral in design, their executive boards are known to be dominated by, and biased towards, developed world representatives. To give significant influence over domestic policy to external agents such as the BW institutions is *prima facie* an abrogation of the democratic expectations of the domestic citizens. It also leads to potential conflict of interest issues as the developed countries which dominate the BW institutions are also the creditors.

The conditions to be met by HIPC countries are determined in Poverty Reduction Strategy Papers (PRSPs). PRSPs are prepared by the debtor country in consultation with domestic interest groups such as business and civil society, as well as consultation with the IMF. It might be argued that since debtor country agencies – both government and civil sector – are involved in forming the PRSP, the BW institutions' imposition of conditions is minimal.

However, the PRSP must be approved by the IMF and WB executive boards. It can be turned down if it is judged to be flawed. Before the PRSP reaches the IMF and WB executive boards for approval, it must pass through a Joint Staff Assessment or JSA conducted by staff from both institutions. At this stage the paper can be modified as the debtor country authority is told of changes which would make the executive board more likely to accept it.

Quite aside from this vetting, the discussion leading to the PRSP in the debtor country is itself circumscribed. Civil society organizations involved in PRSP discussion have consistently reported that there were two parallel processes – one for 'social' issues and one for macro-economic issues. The NGOs were invited to comment on the former, but were not included on workshops discussing the latter (Rowden and Imara 2004: part 2). The social issues largely related to how money budgeted for social services is best spent. The macro-economic issues include privatization, trade liberalization, producer subsidies, industrial policy to promote particular industries, and policy to diversify the economy in specific ways. Overall, the PRSPs which have so far resulted show strong continuity with the structural reform agendas pursued by the IMF over the past decades. Macro-economic policy, in particular, remains the same (UNCTAD 2002: 170ff).

8.4.1.3 The amount of debt reduction is insufficient

Debt reduction advocacy groups such as the Jubilee Debt Campaign suggest that the institutions can afford to give bigger reductions in debt without jeopardising their operations. Given that the institutions are not in the business of profit maximising and are multilateral arrangements for the greatest benefit of all members, campaign groups argue that they should make larger reductions. As befits multilateral agencies, the articles of agreement of the lending arms of these institutions contain provisions for reducing debt burdens owed to the institutions, lengthening the repayment term and lowering interest charged (see Raffer 2007: 98).

This criticism is compounded by the existence of *phantom debts*. If the creditors sold their debt on a secondary market, they would get a far lower price than the face value of the debt. This is because buyers would only pay as much as they expect the debtor will repay. For many developing countries, it is commonly believed

that they will never repay the face value of the debt. The debt burden is simply too great. The *market value* of the existing debt – the price the creditors would get if they sold the debt on competitive secondary markets – is far lower than the face value. This is simply the reappearance of risk in the credit market. The difference between the face value and the market value is phantom debt. Yet, the debt reduction plans are plans to reduce the face value of the debt. Accordingly, while creditors may seem to be absorbing quite a cost by committing to reduce the *face value* of a country's debt by some large percentage, the actual cost they suffer is much smaller. The US, for example, is owed roughly \$6 billion by the HIPC's in bilateral loans. Yet its official accounts hold the debt as being around 10% of the face value, as it expects the rest to be uncollectable (Sachs et al 1999: 10).

8.4.1.4 Unpredictability of debt management hinders long term development planning

Currently, HIPC countries cope with debt service burdens through arrears (failure to pay on time), new loans, grants and rescheduling of loans. These are unpredictable measures which do not lend themselves to being negotiated in advance. They can take up a large part of debtor government's scarce resource of financial planners and negotiators. Moreover, the unpredictability hinders the formulation of long term development plans (Sachs et al 1999: 7-8).

8.5 Proposed reforms

8.5.1 Debt reduction for HIPC's

Various criticisms of the existing HIPC and related initiatives were noted above and foreshadowed an alternative. I contend that HIPC debt should be cancelled immediately and unconditionally. This recognises that the burden of debt is too high in terms of social opportunity cost. It recognises that making the debt merely financially sustainable rather than cancelling it will not solve the problem that there is insufficient wealth for adequate social spending. Cancellation will free up the countries to increase social spending. It will give them more certainty about their financial situation over the near future and thus allow them to plan macro-economic and trade policy in order to pursue development as they choose (Sachs et al 1999: 3-6). It is not certain that all of the available money will flow to poverty alleviation projects, as some of it may end up in the pockets of corrupt politicians. However, I treat this as a separate problem relating to corruption, which must be addressed by other mechanisms. I see no reason why debt reduction, with the *potential* for contributing to poverty alleviation, should be discounted because the potential will not be actualised in all cases. The aim is to remove one reason why the funds devoted to poverty alleviation are insufficient by removing debt service from the list of obligations of certain countries.

8.5.2 Private external debt

It was thought that, generally, private borrowers would only borrow if they could repay and that if there was a problem repaying, only the private borrower would reap the consequences. The East Asian crisis of 1997 changed this belief. That crisis was underlain by excessive private firm borrowing. Creditors refused to roll over their loans and the region fell into crisis (Stiglitz 2006: 231). Often banks offer very attractive rates for *short-term* loans. Credit constrained private borrowers in

developing countries may take advantage of these attractive rates to fund *long term* projects. This is called 'maturity mismatch'. The borrowers then face the problem of *rolling over* the loan – renewing it once the short term is over (Chang and Grabel 2004: 117). With large numbers of firms unable to roll over their loans in a short space of time, the productivity of a country can drop, as can investor confidence in the economy.

At this point, debts owed by private firms were effectively nationalised as the IMF lent affected developing country governments dollars with which to repay creditors. These bail-outs meant that both creditors and the initial private borrowers were let off the hook. Meanwhile, the developing country government, and ultimately the developing country tax payers, footed the bill (Stiglitz 2006: 231). This led to greater national debt for these countries. There is an alternative way of dealing with private external debt which does not foist the debt onto a national government. Private borrowers could simply have defaulted on their loans by declaring *bankruptcy*. If a country does not have adequate bankruptcy mechanisms for its domestic firms, then emphasis should be placed on constructing such mechanisms. Countries must not be pressured by multilateral institutions to bail out private domestic borrowers who are insolvent.

8.5.3 Odious debt

Odious debt is debt incurred by a government that was not democratically chosen. It is unfair to hold responsible the general population of a debtor country for debts accumulated by undemocratic regimes which may well have acquired and retained power by military force. While such loans are undertaken in the name of the country, the money is often siphoned off into the pockets of the undemocratic rulers or is used to perpetuate the undemocratic rule through the purchase of weapons, maintenance of troops or the bribing of potential political opponents.

The motivation of the lender may be political (to buy favour in say, the Cold War, or in contemporary geo-politics) or it may be economic (such as access to rich mineral resources). Private lenders are willing to lend even if they suspect that the borrowing government is acting against the wishes of its populace because they are assured that the debt is owed by the country itself and not by any particular government. They are confident that even if the undemocratic government perishes, the succeeding government – whether democratic or undemocratic – will continue to repay. They are assured of this repayment regardless of whether the undemocratic rulers used the money for the benefit of the population or whether it used it to repress and terrorise the population.

Let me provide some illustration of the politics surrounding odious debt. The US has used the idea of odious debts twice – once with Cuba's debts to Spain, whose repudiation effectively brought the country under US control and not Spanish, and again with Iraq when it was invaded. In both cases US political and economic interest is evident. There are many other countries where similar arguments are available and where debt reduction is similarly justifiable. However, these countries have had no powerful government to champion their cause. In some cases, powerful interests would suffer economic and political cost and so resist odious debt forgiveness. For example, large debts incurred by Zaire under Mobutu, by Nicaragua under Somoza or by Chile or Argentina under fascist regimes can be considered odious for reasons

similar to the case of Iraq's debt under Saddam Hussein. However, US government support of the relevant regimes at the time means a political cost to the US government of allowing the cases to be treated similarly. There are also substantial claims by US creditors in those countries, imposing a financial cost on creditors who are in a position to lobby the US government (Raffer 2007: 99).

8.5.3.1 Discouraging future odious debt

Thomas Pogge suggests a way to discourage the accumulation of such odious debt in the future (Pogge 2002: 153-61). While in a democratic period of government, developing countries should amend their constitutions to include a measure that debts incurred by future unconstitutional governments (rulers who acquire or exercise power in violation of the constitution) must not be serviced at public expense.

Governments of rich countries have often sided with their banks by bringing severe pressure on fledgling democracies to repay debts of past authoritarian rulers. They have exerted this pressure with the help of financial institutions over which they have effective control. However, with such constitutional amendments, governments of rich countries would find such action on behalf of its banks more embarrassing and thus more difficult to justify to its population. It may be that the governments of rich countries are still willing to aid their banks, confident in their public relations skills in convincing the electorate. However this proposal at least creates some uncertainty for lenders as to whether their government will intervene as a last resort and secure repayment of loans to undemocratic rulers of developing countries.

The intended effect of reducing an undemocratic government's ability to borrow should not have the unintended effect of reducing the ability of *democratic* governments to do the same. Loss of constitutionally democratic government is clear in some cases like a military coup. However, it may also be unclear in other cases. For example, allegations that the government engaged in massive electoral fraud, unreasonably postponed elections, excessively limited opposition activity or otherwise greatly exceeded constitutional power are all subject to controversy, whether reasonable or not.

It is inadvisable to rely on domestic courts to settle the issue of whether a government is constitutional, as the opposition may accuse the court of colluding with the government or of being intimidated by it. The risk is that creditors may be reluctant to lend to *any* government of such a country fearing that payment may be reasonably or unreasonably refused in the future on the grounds that the government receiving the loan at the time was illegitimate.

To avoid this, the country should officially empower an external body to settle such issues authoritatively. This external body should not be a group of governments because they may be perceived to have political interests for deciding one way or another on the legitimacy of a government. Instead, the body should comprise an international panel of reputable independent jurists living abroad who understand the country's constitution and political system well enough to judge whether a group's acquisition or exercise of power is constitutionally legitimate.

If many countries initiate such constitutional changes, they can initiate a freestanding 'Democracy Panel' under the auspices of the UN. The Panel would have

sufficient resources to monitor elections and other pertinent developments in the member countries in order to assess whether any of the countries is governed in violation of the country's constitution.

A broadly democratic constitution can, through a sequence of constitutionally legitimate amendments, wind up as authoritarian rather than democratic. A Democracy Panel should resign its authority for a given country at the point where that country's constitution ceases to be broadly democratic.

Another way in which the proposal can have the unintended effect of reducing the ability of *democratic* governments to borrow is this. If an undemocratic government succeeds a democratic one, it may refuse to pay its predecessor's debts. Since it will have a hard time borrowing anyway, it won't burn any bridges by refusing to repay and it will keep more of the existing government revenue. Anticipating this, foreign banks may be more reluctant to lend in democratic periods in a country's history.

This can be handled by establishing an International Democratic Loan Guarantee Fund. This Democratic Fund would temporarily service the debt of a debtor with a broadly democratic constitution as recognised by the Democracy Panel in the event and *only* in the event that unconstitutional rulers refuse to service the debt. The Democracy Fund would cover this cost and expect to be repaid by the country whose costs it covers when that country returns to constitutionally democratic rule.

Note that the unconstitutional rulers are still obligated under international law to repay the country's debt and should be subject to sanctions if they refuse to do this. Thus the unconstitutional ruler still has an incentive to service the debts of its democratic predecessors. The Democracy Fund is in place simply to offset the risk that creditors may be unwilling to lend to democratic governments for fear that the debt may not be serviced by some undemocratic governments.

The Democracy Fund should be backed by many democratic countries, including rich and stable ones, so that it can cover these costs. The stable democracies, unlikely as they are to experience a coup, would probably never benefit from the Democracy Fund. Nonetheless, their contribution to the Fund is justified by the global gain in democracy and the attendant reduction in civil war, war and human rights problems and the resulting reduction in the need to absorb refugees and the need to fund other humanitarian initiatives.

The Fund can be begun without the help of the governments of the rich developed countries if need be, by willing democratic developing countries, progressive developed countries, international organizations, banks and multinational corporations. The establishment of the Fund may be easier if the associated risk is reinsured and securitized. That is, investors could be invited to assume some of the risk in exchange for a fixed premium.

Governments of rich countries will likely agitate against moves to make the proposed constitutional amendments and to set up the Democracy Panel or Democracy Fund. They may do this on behalf of their banks. They may also do this

because they do not want to give up the geo-political tool of buying the political favour of undemocratic leaders or the tool of cheaper access to the natural resources of a country that results when a country is under undemocratic and corrupt rule. They may oppose the proposal professing the concern that the stability of the international financial system requires that lenders be able to rely on governments to repay the debts of their predecessors *irrespective* of what they claim to believe about the predecessor's legitimacy.

In response, we can point out that the constitutional amendment will have no negative effect on the international financial system so long as the rich countries help sustain the full credibility of the Democracy Fund. At the very least, the existence of this response makes more difficult the public relations task of the governments of rich countries if they are to justify their opposition to their electorate.

8.5.4 Sovereign bankruptcy mechanism to discourage future accumulation of debt

The proposal of a sovereign bankruptcy mechanism has been foreshadowed in above sections, especially in criticisms of the status quo. Here I review the comments and describe how the mechanism might work.

To reduce accumulation of debt in the future, a sovereign bankruptcy mechanism can be established. It is beneficial for countries to be able to file for bankrupt status in an orderly way that does not impose large costs for them, and can do so to an independent court not biased by creditor interests. It makes debt reduction and renegotiation a realistic possibility for all developing countries that need it.

In the absence of a legal framework for sovereign bankruptcy, debtors may fear that declaring themselves insolvent or defaulting will drastically narrow options for future loans. The fear is that the debtor must maintain the perception of being credit-worthy in the eyes of potential lenders and that this perception may be damaged by default. There is also the fear of the consequences of default. It has been charged that the IMF has at times intentionally tried to increase the cost of default on its loans, even in unreasonable ways, in order to signal to other debtors that this is an unattractive prospect (see the case of Argentina in Stiglitz 2006: 223).

A sovereign bankruptcy mechanism with a third party arbiter can clarify uniform consequences for debtors and can mitigate imbalances in bargaining power between creditor and debtor. As for the worry about access to sources of credit, most countries with too much debt are likely to have stagnating economies as debt service diverts money away from productive investment. Yet, investors are on the lookout for growing economies, where they can expect a return on their money. The stagnating markets are unlikely to attract creditors, at least not private ones. By contrast, once a country undergoes bankruptcy and its slate is wiped clean, it can use more of the national income for development and growth. Once it starts to grow, it will once again have access to capital markets, regardless of whether the country defaulted. Financial markets are forward looking, caring about the borrower's ability to repay. With full employment and removal of the burden of debt, a default can quickly give way to a net inflow of capital (Stiglitz 2006: 225). This is the general rationale behind all bankruptcy law.

By allowing severely indebted debtors to enter bankruptcy in an orderly way, it is expected that debtors are less likely to undertake new loans to finance arrears and existing debt payment deadlines. Thus, opportunities for governments and multilateral institutions to bail out private creditors can be expected to fall. This should force private creditors to pay greater attention to assessments of risk and should reduce incentives to over-lend.

An adequate sovereign bankruptcy mechanism could be modelled on the US bankruptcy law for municipal bodies, with adjustments to make it more appropriate to an international setting. I present here an outline of the plan from Raffer and Singer 2001 (pp194-6)³⁵.

Chapter 9 of the US bankruptcy code protects both governmental powers of the debtor municipality and the individuals affected by the plan. Affected tax payers as well as employees of the municipality have a right to be heard, to defend their interests. Creditors are to receive 'what can be reasonably expected from the debtor under the circumstances'. The living standards of the inhabitants of the municipality are protected. The jurisdiction of the court depends on the debtor's volition, beyond which it cannot be extended.

Extending this to the case of sovereign debt, minimum standards of living in the debtor country must be protected. For example, the money owed must not be raised by destroying basic social services. Subsidies and transfers necessary for the well being of the poor must remain. Funds needed for sustainable economic recovery must be set aside. Counsel from groups such the World Health Organisation, the Food and Agricultural Organization, the World Food Program, UNICEF and the Joint UN Program for HIV-AIDS should be sought in judging the social needs of citizens in the debtor country. Such counsel can inform estimates of the spending required to adequately tend to these social services and of the types of programs required (Sachs et al 1999: 11).

In addition, the arbitration and judgment of the amount of debt reduction and thus the amount of cost to be borne by the creditor should take into consideration facts such as whether the loan was made with full knowledge of the high risk and the interest rate charged. If the interest charged was high enough, the principal may be repaid quickly, so that all repayments after that are purely profits. It should also be taken into consideration whether the lender was partly culpable for the problems facing the debtor. We have discussed some sorts of liabilities already which are relevant here. With the BW institutions, there is also liability if the debtor country's trouble was worsened by its implementation of policies that were conditions of receiving the loans from BW institutions.

It may be necessary to demonstrate that the money set aside will be used *as claimed*. The solution is a transparently managed fund financed by the debtor in domestic currency. Proposals for the design of such a fund exist. For example, Ann Pettifor, in a discussion with BW institutions and public servants of G7, proposed a Poverty Action Fund to ensure that the money is actually used for the poor and for the fresh start of the country (Pettifor 1999). The management of the fund would be an international council with members from both creditor and debtor countries,

³⁵ See also Raffer 1990 and (Raffer and Singer 1996: 203ff). Demands for a sovereign bankruptcy mechanism are made by many in the literature. See for example (Stiglitz 2006: 233ff).

nominated by NGOs and the debtor government. This fund is a separate legal entity to the debtor's government and so has no relation to its budget.

In the interests of fairness and to avoid bias, the adjudicating court must not be based in either the lender or debtor country. An international court is needed. Each side would nominate the same number of persons who pick one more person to constitute an odd numbered adjudicating group. Those affected are represented by organizations which speak on their behalf – trade unions, international organizations, NGOs and grassroots groups.

Debt service payments need to be brought in line with the debtor's capacity to earn foreign exchange. Where removal of protectionist barriers by the creditor country is likely to lead to increased export revenue for the debtor country, a trade-off is necessary between greater repayments combined with lower protections on the one hand and greater debt reduction without reduced protections on the other.

Official creditors, including IFIs, must be treated just as any creditor is in usual insolvency proceedings. Especially so as they, (unlike private creditors), have often decided how their loans were to be used. There must be symmetrical treatment of all creditors – the same percentage being reduced from all loans. This could be the way that BW institutions are held financially accountable for the loans they make as well as for the conditions they attach to them, as they have so far been reluctant to suffer any reductions in repayments while urging private and bilateral creditors to do so. This reflects the fact that an independent party, rather than the BW creditors, would administer the bankruptcy proceedings. This also lessens the ability of BW institutions to demand further conditionalities in exchange for new loans in debt management. Given that troubled indebted countries can turn to a bankruptcy mechanism, they may be less likely to undertake new loans and thus less likely to be bound by conditionalities. This addresses another egalitarian worry about the domination of debtor country policy by external sources, the external sources being the BW institutions and the means of domination being the conditionalities.

One possible objection to some of the reforms considered here is that they will dry up the flow of affordable loans to poor countries. If conditions become harsher for lenders, then lenders face more risk. Conditions become harsher for lenders if debtor countries, and private debtors in poor countries, can file for bankruptcy. Lenders are no longer assured of bail-outs, or of continued debt service financed by the undertaking of new loans. It is unclear how widespread a problem this is, but it is likely to be a problem at least for some countries. Alternate sources of funds for poor countries must be considered. I mention some possibilities for generating a steady stream of revenue for poor countries, or for their citizens. Possibilities include a Global Resources Dividend (Pogge 2002), or a Tobin tax on international currency exchanges (Tobin 1996), (Rafffer and Singer 2001: ch 14). Another possibility is discussed in passing in the next chapter (chapter 9). The alternative system of global reserves considered in chapter 9 allows allocation of reserves in a progressive way and also collects a tax on the trade surplus of a country which can then be distributed progressively. Both the allocation of reserves and the surplus tax generate flows which can be channelled to poor countries to replace any decrease in availability of loans due to the reforms proposed in this chapter. These various proposals are sources of *grants* rather than of loans to poor countries.

The institutions surrounding sovereign debt are relevant to egalitarians for various reasons. They contribute to global *poverty* and under-development since debt service extracts money out of a poor country that could have been used to alleviate poverty or to fund domestic productive investment and economic growth instead. The absence of a sovereign bankruptcy mechanism is *unfair* for the debtor countries and for their citizens, as it makes it harder for heavily indebted countries to negotiate with creditors to reduce the burden of debt service. The behaviour of creditor governments and of multi-lateral institutions is partly responsible for the heavy debts of many countries for reasons noted in section 8.2. Again, the effects of such behaviour could have been mitigated by the use of adequate bankruptcy mechanisms for both debtor countries and for private debtors in developing countries.

I considered two sorts of proposals. One is to reduce debt for some groups of countries: the heavily indebted poor countries, and countries that owe odious debt. Two, I considered some proposals to reduce the future accumulation of debt: better bankruptcy mechanisms for private firms in developing countries, the Democracy Panel in relation to odious debt, and the sovereign bankruptcy mechanism. The bankruptcy mechanism applies to all debtor countries. The Democracy Panel and the sovereign bankruptcy mechanism also address egalitarian worries about the unfairness of existing institutions.

In terms of the positive duty/ negative duty distinction discussed previously in chapters 4 and 5, this latter point makes remedial change a matter of negative duty on the part of the developed country governments and (to some extent) their citizens. These agents and collective agents have the negative duty to refrain from committing acts that perpetuate institutions that aggravate accumulation of debt, since the accumulation worsens the poverty of some residents of indebted developing countries. The acts they commit include perpetuation of a system of sovereign debt management that does not have bankruptcy protections for debtors, and of a system that holds populations responsible for debts incurred by undemocratic rulers on their behalf.

This ends my discussion of international debt. Let me introduce the topic of the coming chapter. Much difficulty in meeting debt repayments is due to instability of the global reserve system. In order to properly address the issue of debt, we must also address the global reserve system. Let me move on to a discussion of that system. The coming discussion of the global reserve system will not be limited to links with international debt, however. Instead, it will consider the nexus of issues surrounding the reserve system itself. I want to build the strongest case for reform of the reserve system and doing so requires assessing various undesirable features of the existing system and not merely the undesirable consequences for debt repayment.

Chapter 9: The Global Reserve System

There are two major reasons why the global reserve system (or GRS) is relevant to an egalitarian investigation of global poverty. One, the existing reserve system diverts some developing country resources away from development projects and poverty eradication. Two, the GRS contributes to global economic instability. If less were diverted into reserves, this would free up a lot more of developing country money. As for economic instability and crisis, these can affect poor and developing countries particularly severely. These countries may have to acquire large debts to spend themselves out of the crisis. In the previous chapter, I described the potentially harmful effects of large debts for poor and developing countries. Developing countries also tend to have poor social safety nets, meaning that bouts of especially high unemployment during an economic crisis can send people into abject poverty. Rectifying the harmful effects of the existing system would thus help developing countries considerably.

The discussion of the global reserve system culminates in a proposal for its reform. On the way, I will present background information about the purpose of reserves, how reserves affect the economies of various countries and the costs and benefits of the existing system.

In section 9.1, I outline the reasons why countries hold reserves. In section 9.2, I describe the effects on the US – the economy of the main reserve currency – of the existing reserve system. I rely on work by Bruce Greenwald and Joseph Stiglitz to make this case. In section 9.3, I consider effects of the system on developing countries. This section clarifies why this issue is of concern to egalitarians. I discuss the opportunity cost of holding reserves in section 9.3.1, and the cost in terms of greater global economic instability in 9.3.2.

In section 9.4, I describe some reforms proposed by Greenwald and Stiglitz. Section 9.5 explains how the reforms could help the developing countries.

9.1 Reasons for holding reserves

Reserves are large amounts of wealth held by governments. This wealth is held in forms considered to be widely acceptable as a store of value even if the fiat currency of a country becomes less acceptable. Historically, gold has been a material very widely accepted as a store of value, sometimes perceived to have intrinsic value. Fiat currency is a store of value and a means of exchange which is deemed to have value as a matter of fiat. This includes paper money, for example. It was thought that fiat currency only had value insofar as it could be converted into an equivalent amount of something which is more widely accepted as a store of value – such as gold or, more recently, strong currencies such as the US dollar.

Initially, fiat money was backed by an equivalent amount of gold. For each paper dollar circulating in the economy, the government would hold a dollar's worth of gold, from which the paper derived its value. Later it was realised that this sort of one-to-one convertibility was unnecessary. All that is required *is confidence in the currency* in the sense that others would be willing to accept the fiat money as payment. This confidence could be achieved with only partial backing rather than one-to-one backing. Confidence in a currency means that economic agents are willing

to accept and trade the currency. Partial backing of a currency, rather than one-to-one backing, rests on the following general fact. Generally, demand for a currency will always be high enough that at any one time holders of the fiat currency will want to exchange only a small fraction of the total stock of the fiat currency in circulation for a more acceptable form of wealth (say, gold).

Initially it was thought that confidence would only result if gold was used for backing. Then it was realised that the currency or debt of strong economies (once UK, now US) could be used instead. Debt of a strong economy can be held as a reserve in, for example, the form of a Treasury bill or T-bill issued by the US Treasury. What matters for the purpose of reserves is not the *form* of the wealth in which the reserves are denominated, but rather that, whatever the form, it should have the feature of being readily acceptable when the domestic currency is not.

A T-bill entitles the holder (in the case of reserves, the holder is a foreign government) to repayment of the amount lent to the Treasury as well as some small amount of interest upon maturity. Since confidence in a strong economy is high, the debt or Treasury bill is widely acceptable as those buying the Treasury bills are happy that the Treasury will repay the debt upon maturation. Those who acquire T-bills are *lenders* to the US Treasury, as they purchase the T-bill with money and the sum must be repaid with interest upon maturity. Lenders to the US have historically also been confident about the stability of the value of the US\$ - that inflation will be low and that the exchange rate will be stable. This assures lenders that when they are repaid in dollars, the real value of the repaid sum will not be drastically lower than the real value of the amount lent at the time of lending.

There are also other reasons for holding reserves. Let me list a few. Reserves help a country manage risks it faces and this bolsters confidence in both the country's economy and in its currency. Reserve can be drawn upon in time of need. They are a buffer against unexpected changes in the cost of debt service caused by rises in interest rates. Overseas debt is generally denominated in hard currency – the currency of a strong economy, such as the US\$. A reserve of hard currency accommodates sudden rises in interest rate on loans.

Sudden hardships such as crop failure may befall a country. Such an occurrence would force the country to import essential food using the reserves. Historically developing countries held reserves to cover 3-4 months worth of imports, but more recently they have begun holding as much as 8 months' worth (Stiglitz 2006: 247).

Many countries have borrowed short term in hard currency. Fear about the country's economy can make creditors demand immediate repayment of loans. Such demands, though rooted in the fear of an economic downturn, can themselves precipitate a downturn. Demands for immediate repayment result in insufficient funds for planned investments and government spending. As a consequence, aggregate demand falls, leading to an economic downturn. The aggregate demand of an economy is the identity $AD = C + I + G + NX$, where C is total consumption spending, I is the total investment by firms, G is total government spending and NX is **net exports** (that is, money received for exports minus money paid for imports).

A substantial hoard of reserves bolsters creditor confidence in the economy and lowers the risk of creditor panic as creditors think that if the economy turns sour, they can still be repaid out of the reserves. In case of a demand for repayment, sizeable reserves place a country in a better position to repay. Prudence requires countries to maintain the larger of (i) enough reserves for a few months of imports and (ii) enough to match all short term debt denominated in hard currency (Stiglitz 2006: 247).

Lack of money for essential imports such as food staples and sudden demands for repayments of short-term loans are among the more serious economic crises that can hit a country. The first can result in widespread malnutrition or starvation while the latter can plunge a country into severe recession. The prudential guideline thus allows some security against these very harmful possibilities. This guideline will feature in the alternate reserve system I present below.

Reserves can also be used to manage the exchange rate. Speculators or currency manipulators can sell or buy a currency very fast and drive down its value. Reserves allow the government to buy or sell to counteract this activity in currency markets to maintain relative stability of the exchange rate. They can only counteract if they have reserves of hard currency with which to buy the domestic currency (Stiglitz 2006: 247).

9.2 Effects of the existing reserve system on the economy of the main reserve country

When US government expenditure exceeds its tax revenue, this is financed by issuing government debt, generally in the form of bonds sold on an open market. Some of the debt can be *monetized*. Monetizing is a process whereby the US Federal Reserve agrees to create new money with which to buy some of the government issued bonds. The Federal Reserve considers the bonds as an increase in its assets against which it can increase its lending. Through this increased lending, the economy experiences an increase in the money supply. The effects of monetizing are that the increase in money supply contributes to inflation and to depreciation of the currency's exchange rate, while the increase in lending lowers interest rates.

When the US government has a fiscal surplus, it can use this to pay down its outstanding debt (whether debt owed to foreigners or to domestic lenders). It can do this by paying maturing bonds while not issuing new bonds at the same time. It can also purchase its bonds on the open market even if they are not due for redemption.

Technically the US cannot go bankrupt as it can always print new money to pay its debts. However, if there is a great imbalance between the amount of money in circulation and the amount of economic goods represented in the economy, the risk of hyperinflation arises. Hyperinflation is characterised by the following sorts of occurrences: a loss of confidence in the currency so that people are unwilling to hold that currency and prefer to convert any holdings to physical assets or to foreign currencies which are more stable in value or to specie such as gold which is more stable in value; an increase in the supply of money which outpaces demand for the money; an expectation among producers that there will be continued and significant inflation so that they set short term prices higher in order to account for this

expectation – this feeds further inflation as prices rise; there may be a decline in the economy as investors are less willing to invest in the economy and take their investments abroad.

Even if bankruptcy may not be a consequence of excessive debt for the US, there are other potential bad consequences. Hyperinflation and loss of confidence in the currency can be devastating for the US economy.

Inflationary pressure has been mitigated in recent years, as China has been willing to accumulate US denominated assets, absorbing masses of debt issued by the US. If the increase in money supply were not offset by an increase in demand, then the value of the money would fall (that is, there would be inflation). With foreign countries demanding the dollar and dollar denominated debt for their reserves (China being the chief such country), the inflationary pressure has been mitigated.

9.2.1 The global reserve system as a contributing factor in the chronic US trade deficit

The US has had a chronic trade deficit since the 1970s. Debate around possible causes of this has not reached unanimous conclusion, but among the proposed explanations is the current global reserve system. The reason I discuss this is that it is important in building a case for why the reserve system should be reformed. In particular, the explanation linking the reserve system and the chronic trade deficit in this section will contribute to the following section where I discuss ways in which the reserve system renders the global economy less stable.

Let me follow Greenwald's and Stiglitz's explanation of the issue (Greenwald and Stiglitz 2006). Let **NFS** be the net foreign surplus. This is the total of both private and public investment overseas. Purchase of Treasury bills by the government of a foreign country counts as such public investment (bringing the return of the 1-2% interest rate) for our purposes. Let **I** be domestic investment, let **NPS** be net private savings by households and firms and let **NGS** be net government savings (that is, the net budget surplus).

In a national economy, net foreign surplus (**NFS**) must equal net private savings by households and firms (**NPS**) plus net government savings (**NGS**) minus domestic investment. We can represent this as

$$\text{NFS} = \text{NPS} + \text{NGS} - \text{I} \quad (1)$$

If domestic investment exceeds the sum of **NPS** and **NGS**, then it is being funded by borrowing from overseas – that is, by a foreign deficit. To restate the point, if **I** is greater than **NPS+NGS**, the right hand side of equation (1) is negative, making **NFS** negative too (a negative net foreign surplus is a foreign deficit). Likewise, if **NPS+NGS** exceeds domestic investment, then the remaining savings go overseas, constituting a positive net foreign surplus.

The foreign surpluses and deficits of all countries in the world sum to zero. To consider the international monetary system as a whole, let the subscript **T** designate a

sum over all individual economies. Then this fact about the international monetary system can be represented as:

$$\mathbf{NFS}_T = \mathbf{NPS}_T + \mathbf{NGS}_T - \mathbf{I}_T = 0 \quad (2)$$

In our current system divided into a reserve currency and non-reserve currencies,

$$\mathbf{NFS}_T = \mathbf{NFS}_R + \mathbf{NFS}_N = 0$$

where subscript **R** denotes reserve currency country and subscript **N** denotes the sum of balances for the non-reserve currency countries.

This allows us to write

$$\mathbf{NFS}_R = \mathbf{NPS}_R + \mathbf{NGS}_R - \mathbf{I}_R = -\mathbf{NFS}_N = -\mathbf{NPS}_N - \mathbf{NGS}_N + \mathbf{I}_N \quad (3)$$

The US has a chronic foreign deficit which began in the 1970s. The literature discussing this chronic deficit advances different causes of the deficit. One view is the ‘**Twin Deficits**’ view. It holds that the imbalance is driven by fiscal deficits by the US government and by a low savings rate. That is, small **NPS_R**, large and negative **NGS_R**, and relatively large and positive **I_R**. This gives a large and negative **NFS_R**.

This describes some of the internal workings within a country – if domestic investment exceeds the sum of net budget surplus and net private savings, then investment is partly being funded by overseas borrowing. However, for the US, empirical data argues against this view of national behaviour as the *predominant* factor. Correlation between fiscal deficit and current account deficit is minimal. US government deficit rises steadily from the early 1970s to the late 1980s, begins to decline in the 1990s, changes to a surplus in 1998 and rises sharply after 2000. By contrast the current account deficit grows steadily throughout. Further, if fiscal deficit is generally a strong factor in current account deficits for individual countries, there should be some correlation across countries between fiscal deficits and current account deficits. The correlation is, in fact, almost non-existent (Greenwald and Stiglitz 2006: 3).

A second view of the causes of the US chronic trade deficit is the ‘**Savings Glut**’ view. The Twin Deficits view looked at domestic factors affecting net foreign surplus in equation (1). The Savings Glut view looks at international matters and at equations (2) and (3). It notes that **NFS_N** is strongly positive. This, in turn, is because high private savings **NPS_N** and low government deficits are not offset by comparably high rates of investment. That is, there is insufficient investment by non-reserve countries in non-reserve countries, so the money available for investment enters the US instead. There is a net glut of domestic savings in non-reserve countries which must be deployed overseas. On this view, the strongly positive net private savings of the rest of the world drives the offsetting US **NFS** to be strongly negative.

While this may be a partial explanation, it is not very promising as a complete story. US trade balance has been in deficit since the 1970s. The savings glut explanation would require that this chronic deficit is due to a constantly increasing global savings glut since the 1970s. Yet it is not clear why, *in the long run*, there should exist this structural imbalance between savings in the non-US world and investment in the non-US world. If there does exist such a persistent difference, we would expect it to be overcome on a country by country basis by appropriate national fiscal and monetary policies. Individual governments might lower interest rates to encourage greater domestic investment so that more of the savings remain in the country. Or the government might undertake more public spending domestically, again, using up more of the savings domestically.

Greenwald and Stiglitz propose an alternate view of the causes of chronic US trade deficit since the 1970s. We have noted several reasons for holding reserves. As the volume of international transactions grows, so does the desired volume of reserves. For example, larger reserves are needed to manage the exchange rate, or to protect against unexpected demands for short term debt repayment or to cover essential imports. So, given the rising volume of transactions, we expect that the total volume of reserves will rise.

For there to be an addition to a country's reserves, its NFS must be positive. Desired NFS_N will be positive and will therefore push the reserve country towards a negative NFS_R , that is, a deficit. Let me present in somewhat greater detail the grounds for believing that desired NFS_N will be positive.

NFS is composed of both private surplus and public surplus. (Note that we are now talking about private surplus and public surplus, not about private savings and government savings.) Consider the private surplus component. The desired private foreign surplus consists of the difference between desired overseas investment by domestic agents and desired foreign investment in the country. Many developing countries these days seek foreign direct investment (FDI) in order to fund development. If FDI entering a country exceeds the direct investment by the country's private agents in foreign countries, then the country's net private surplus is negative.

However, as we have seen, governments tend to seek larger reserves for security as more FDI flows into the country. This is to reassure the foreign investors of the country's ability to repay. For a government to add to its reserves, the country's net public surplus must be positive. This desired addition to reserves is as large as the FDI flowing into the country. Now consider the aggregate of non-reserve countries. The FDI flowing into these countries (with a negative effect on each country's net private surplus and thus on its NFS) is countered by the country's desired addition to its reserves (with a positive effect on its net public surplus and thus on its NFS). At the aggregate level, even if desired private surplus across all non-reserve countries is negative, the desired public surplus will be positive and sufficient to cancel out the desired private surplus. Moreover, there will be other reasons for desired additions to reserves. The combined result will be that desired NFS_N will be positive, due in large part to the desire for reserves. As long as non-reserve countries achieve their desired levels of reserve accumulation, the reserve country is faced with chronic deficit.

Non-reserve countries can achieve their desire for larger reserves by running trade surpluses. The excess of export receipts over import payments can buy US Treasury bills to boost reserves. Ways in which countries can seek trade surpluses include favourable tax and regulatory treatment of export industries, impediments to imports and ER management, to depreciate the currency and make exports more attractive.

Of course, the reserve country can refuse to run the required deficits and thereby fail to fund these through the issuance of T-bills. In that case, the methods mentioned above for trying to boost reserves will not boost the aggregate of non-reserve countries' reserves. Instead, the non-reserve countries will compete over an inadequate overall supply of reserves. If all countries seek to simultaneously devalue their currencies, none will succeed. The competition for reserves may result in increasing barriers to trade and competing domestic deflation (trying to attract export demand). These would, in turn, lead to reduced import demand as imports become dearer, affecting the trade partner's aggregate demand.

The East Asian crisis of 1997 is an example of this phenomenon. Persistent current account deficits in several East Asian countries led to a loss of investor confidence and capital flight from those economies, depreciating currency and growing debt. Eventually, the combination of low exchange rate and low import demand moved the countries into net foreign surplus. Foreign surpluses are offset by foreign deficits in the zero-sum international monetary system. So, for these countries to move from deficit to net foreign surplus, other countries necessarily had to move to greater deficit.

If the US does not offset these new surpluses by increasing its deficit, other economies will have to move into greater deficit. In the East Asian crisis, the deficit moved to countries such as Russia, Brazil and Mexico. Thus, in the absence of sufficiently high deficits by the reserve country, the reserve country global reserve system is unstable, carrying the possibility of economic downturns which can spread from country to country as affected countries reduce their demand for imports from trade partners and impose trade restrictions.

A growing volume of international transactions means that non-reserve countries want to hold growing amounts in reserve. There are then two possibilities – one, the aggregate of non-reserve countries' desire for greater reserves is satisfied, or two, the desire is not satisfied. If the aggregate of non-reserve countries' desire for reserves is satisfied, this can only occur because the reserve country increases its deficit and issues more debt. If the desire is not satisfied, the non-reserve countries compete for an insufficient supply of reserves by trying to attain and maintain trade surpluses. A non-reserve country does this by such means as import restrictions and exchange rate management. These means lower aggregate demand for trade partners, as the non-reserve country lowers its demand for imports from its trade partners. This lowering of aggregate demand is a deflationary bias in this global reserve system.

Chronic and growing reserve country (US) deficits are an inherent part of the system for maintaining stability by avoiding continual deflationary pressure on economies.

This imbalance can be worsened by factors additional to the desire for reserves to keep pace with growing international transactions. One, there is a basic imbalance at the heart of this reserve currency system. Trade deficits are somewhat self limiting in the sense that non-reserve countries run out of reserves with which to pay for trade deficits year after year, or they face the heavy cost of continually acquiring debt to fund the deficits. Countries with chronic trade surpluses face domestic inflationary pressure of surpluses which comes in the form of the constant boost to AD through exports and constant appreciation of the currency. However, so long as they neutralize this pressure, they can continue to run annual trade surpluses indefinitely. In a world of flexible exchange rates, countries can fight upward pressure on their exchange rates by increasing the supply of their currency on the market.

Two, for idiosyncratic reasons individual countries may be committed to producing trade surpluses beyond their need for reserves. China, for example, uses surpluses as an engine for output growth, given that its monetary and fiscal policies are inadequate to manage its macro-economy locally. Japan seems to regard itself as a vulnerable economy dependent on its ability to export manufactures. This leads it to policies producing persistent net foreign surpluses which must be absorbed elsewhere in the world. In Europe, powerfully entrenched interest groups in manufacturing and agriculture have been protected over the years in ways that have generated large and persistent **NFS**. In agriculture this is via restricting import competition.

I should clarify that this is an idiosyncratic matter concerning the autonomous behaviour of some countries, and not a systemic matter inherent to the reserve system. Let me stress, however, that even if the countries did not act thus, the problematic imbalance would persist, because of the systemic reasons I have presented above. Those above reasons constitute my substantial criticism of the reserve system and are my motivation for advocating an alternate reserve system. This is to forestall rejoinders that any problems with the reserve system can be easily rectified without need for drastic change to the global reserve system, if only a handful of culpable countries would change their ways.

Three, some countries – like Korea, Thailand and Indonesia –have suffered persistent deficits and have borne the related costs. Such countries are likely to now seek persistent surpluses to guard against the costs, putting pressure on other economies to offset this by undergoing deficits.

9.3 The effects of the existing reserve system on developing countries

We have examined some reasons for holding reserves. However, there are also costs to holding reserves which weigh against the benefits of holding them. Before describing these costs, let me first give an indication of the size of the global pool of reserves. The size of reserves held globally matters because the costs of holding reserves are magnified depending on the size of global reserves.

The size of reserves held by countries has increased greatly in recent times. Between 2001 and 2005, eight East Asian countries more than doubled their total reserves. The countries – Japan, China, S. Korea, Singapore, Malaysia, Thailand, Indonesia and the Philippines – increased their total reserves from around \$1 trillion

to \$2.3 trillion. China alone had about \$900 billion in reserves by 2006 – which amounts to over \$700 for every inhabitant of the country. To put this into perspective, the annual per capita income of China is under \$1500. For developing countries as a group, reserves have risen from 6-8% of GDP in the 1970s to almost 30% of GDP in 2004 (Stiglitz 2006: 248).

Among the causes of this increase are the following two. One, the very high level of global economic and financial instability – which I will discuss later – and two, the way in which the IMF handled the 1997 East Asian crisis. The IMF attached certain conditions to the loans it made to the countries experiencing crises at that time. Those conditions are widely acknowledged to have worsened the economic downturns of the affected countries. Many of the East Asian countries learnt lessons from the crisis and are boosting reserves to draw upon in times of need so that they do not have to borrow from the IMF instead (Stiglitz 2006: 248).

9.3.1 The cost of reserves for developing countries

There are large costs to developing countries of holding reserves. For the most part, reserves are held in US Treasury bills or T-bills³⁶. T-bills earn a meagre real interest rate (that is, an inflation adjusted interest rate) of around 1-2% or even lower. It is possible for T-bills to offer such meagre interest rates as continued demand for T-bills is assured because of the status of the US\$ as the major reserve currency. Meanwhile, most developing countries are cash strapped. They have a choice of many high-return projects, if only they could raise some money to invest in them. Were they not using their money to buy US Treasury bills to build reserves, the money could instead fund these high return projects and earn somewhere in the region of 10-15% (Stiglitz 2006: 249). The difference between the two interest rates can be seen as the opportunity cost to developing countries of holding reserves. Let us place this opportunity cost into context.

Supposing an estimated 10% difference between the two real interest rates, the cost to developing countries of holding reserves is more than \$300 billion annually (developing country reserves total in excess of \$3 trillion). This amount is four times the level of foreign aid from the whole world. It corresponds roughly to estimates of what is needed to achieve Millennium Development Goals, including the halving of global poverty.

Another striking way to put the cost of reserves into context is this. Suppose a firm in a developing country borrows \$100 mil for a short term from a US bank at, say, 20% interest. We noted above in discussing reasons for maintaining reserves that it is advisable to maintain the larger of (i) enough reserves for a few months of imports and (ii) enough to match all short term debt denominated in hard currency. So, suppose the developing country follows this advice and increases its reserves by the amount of the short term loan, namely by \$100 mil. It does this by purchasing \$100 mil worth of Treasury bills at, say, 5% interest. In this case, there is no net flow of funds from the US to the developing country. Moreover, since the US loan charges

³⁶ In my discussion of the global reserve system, I will generally talk of the US\$ as *the* reserve currency rather than as one of the reserve currencies (and the main such currency by a long way). This simplification does not affect the cogency of the argument to come.

a much higher rate of interest that the Treasury bills pay, there is a net transfer of \$15 mil from the developing country to the US.

Having discussed the costs of the existing system to the developing countries, let me note that the main beneficiaries of the existing global reserve system are those countries whose currencies are the reserve currencies. Given that globally, reserves are overwhelmingly (but not solely) held in US\$, the main beneficiary is the US. The existing system is advantageous for US banks and for the US economy more generally. US banks enjoy a large and steady demand for loans from the developing world. The US economy benefits from the injection of loans in the form of issuing of T-bills. The Treasury receives money for the bill it receives and agrees to pay an interest rate plus the principal upon maturation of the loan period. The system allows the US to borrow vast sums of money at very low cost – real interest rates of Treasury bills are, as we have noted, around 1-2% or even less.

However, the developing country does not fare well. The desire to maintain sufficient reserves to guard against economic instability leads the country to divert much needed money for development to instead build reserves. At the same time, this is also effectively a transfer from the public sector in the developing country to the private sector in the same country. The private sector is better off, able to borrow the \$100 mil. Yet the public sector now has a smaller pool of funds for public expenditure (Stiglitz 2006: 249-50).

Of course, there are benefits for the developing country, since the addition to reserves improves the economy's resilience to instability. The point to note, however, is that an alternative global reserve system which maintained stability just as well but which did not require as large an accumulation of reserves on the part of the developing country would be preferable on that count. Under such an alternate system, the developing country would be able to keep more of its money for its own development rather than as a shield against economic instability. We will discuss Stiglitz's proposed alternative global reserve system below.

9.3.2 Cost of the existing system in terms of global economic instability

The deflationary effect makes itself felt in the reserve currency economy as the continuous pressure to run trade deficits means a drag on aggregate demand (remember aggregate demand is $AD=C+I+G+NX$ and NX or 'net exports' is negative in a trade deficit, where imports exceed exports). The reserve country fights this pressure by aggressive fiscal and monetary policy in an attempt to boost aggregate demand by affecting government expenditure and investment. In non-reserve countries, outside of crisis times, the opportunity cost of accumulating large reserves is that they now spend less domestically, meaning that aggregate demand is lower. On a worldwide level, this has to be offset by the US demand for imports.

For these countries, the deflationary pressure erupts occasionally in the form of events like the East Asian crisis, where economic crisis or slowdown spreads from one country to its trade partners. A country facing economic crisis may have insufficient reserves and may be forced to borrow overseas. The loans may be necessary to repay flighty creditors and investors or the government may use the

money to spend its way out of a recession. Thus, recessions can contribute to growing sovereign debts.

The self-defeating nature of the reserve currency system is that the reserve country gets increasingly into debt as it has chronic and growing net foreign deficits to satisfy the rest of the world's demand for reserves. The large and increasing debt of the reserve country comes with a growing risk of inflation – a reduction in the buying power or real value of the dollar. As one of the features which make a currency desirable as reserve is the stability of its value, the inflation, especially if sudden or large, makes the currency less attractive as a reserve.

Traditionally Central Bankers focused on inflation, an attractive reserve being one whose value in terms of goods it can buy is not greatly eroded over time. However, for those outside US, the dollar exchange rate is also a very important determinant of the value of the currency as a reserve. The US\$ has been increasingly volatile in its exchange rate. For example, in a few months in 1995, the US\$ lost 20% of its value against the Yen. While there had been little inflation in the US, those in Japan who had their money in US\$, found they were suddenly less wealthy. Between Feb 2002 and Dec 2004, the US\$ fell against the Euro by about 37%. These are very substantial declines in the value of the dollar which have put an end to the once widely held notion that the dollar was unassailable and very secure as a store of value. As a result, the currency is less attractive as a reserve. In early 2005, China announced that it was no longer committed to reserves in dollars. It had already moved about ¼ of its reserves out of dollars. Central Banks in many other countries are also quietly moving away from dollar holdings (Stiglitz 2006: 255-6).

As US debt rises, so do doubts about the soundness of the dollar. As the value of the dollar falls, investors with assets denominated in US\$ will be better off converting their assets to some other currency. They will convert their money into strong currencies of vibrant economies, including Euros, Yen, and Yuan. Thus there will be a downward pressure on the dollar. At the same time, investors will pull out of US securities as the depreciating dollar will lower returns. US stock prices will fall or stagnate as demand for US stock stalls or falls. This further weakens the US economy and reinforces the decreasing appeal of the dollar.

Turning to Central Banks, as they reduce their holdings of dollars, the supply of dollars on the market increases and this sends its price even lower. This spreads further concern among Central Banks that the value of their reserves is falling (as the value of the dollar is falling) and can trigger a self-reinforcing rush to liquidate dollar holdings. Such a rush can be very dangerous both for the US, as its currency plummets in value, and for countries holding dollar reserves as the value of their holdings plummet. The move out of dollar holdings may be smooth and drawn out or it may be a sudden crash.

That the reserve currency, the US dollar, might suddenly lose its value as the supply of it increases in the world, is a possibility which has been recognised and feared for several decades. A countervailing consideration which has so far kept the value of the dollar more stable than it otherwise might have been is the interest of holders of US currency and debt. Central banks which maintain much of their wealth in US currency or debt have an interest in the strength and stability of the US dollar.

For, if the dollar suddenly loses some of its value, the central banks would also lose some of their wealth (the wealth denominated in US dollars). So, they continue to buy up the available dollars in sufficient amounts so that the dollar's value remains high. They can continue to buy dollars even as they buy other currencies for their reserves and even as they increase the ratio of other currencies to dollars in their reserves. There is no guarantee however, of how successfully and how long these Central Banks can continue to prop up the value of the dollar.

As confidence in the dollar as a stable store of value is diminishing, demand for other currencies as reserves has increased. In particular, demand for the Euro has increased. Europe was initially quite happy to see its currency rise against the dollar, wanting respectability for the Euro and eager for it to be the new reserve. However, as the Euro becomes the new reserve, demand for it rises, increasing its value. This makes European exports less attractive and opens Europe to a flood of imports. Accordingly, it will have an even harder time maintaining full employment. Given that European Central Banks are charged with a focus on inflation and not unemployment or growth, and given that the unemployment there is already problematically high, this does not bode well (Stiglitz 2006: 256). Enthusiasm within the Euro community for the appreciation of its currency has waned, precisely for these reasons. A possible move to another currency as reserve comes with the same problems, simply transplanting them to another economy.

9.4 An egalitarian proposal for reform of the global reserve system

I noted at the start of the chapter that there are two major reasons why the global reserve system is of concern to an egalitarian investigation of global poverty. The existing GRS contributes to global economic instability and the accumulation of reserves diverts developing country income away from poverty alleviation programs. To recap, the instability inherent in the existing reserve system is this. There is continual deflationary pressure on both the reserve country and on non-reserve countries. This deflationary pressure threatens to erupt as recession in a country and to infect economies of trade partners. The gradual erosion of the value of the reserve currency and of the confidence of others in both the economy of the reserve country and in its currency as a reserve threatens to erupt in a sudden devaluation of the reserve currency which can, at worst, cause a worldwide depression. A severe recession can lower national income and raise unemployment. The unemployed in a developing country experiencing recession may fall into abject poverty in the absence of social safety nets.

In protecting themselves against the possibility of economic crises, countries hold reserves. Yet large reserves are especially costly for developing countries as the scarce money is diverted away from poverty alleviation projects and from socially useful investment projects. In addition to reserves, countries may undertake loans to counteract recessions and mitigate crises.

Given the opportunity costs for the global poor when their governments hold large reserves or acquire debt, there is cause for investigating possible reforms of the global reserve system which could contribute to greater global economic stability and reduce pressure on countries to accumulate large reserves. There are many possible

reforms to the GRS. These range from relatively small-scale changes such as individual countries changing their behaviour within the existing GRS to larger changes of the reserve system. I consider one particular proposal for reform, advanced by Greenwald and Stiglitz.

An ideal global reserve system would have stability in terms of exchange rates. It would not be prone to sudden crises. It would also be balanced, in the sense that national economies should face neither a deflationary pressure from chronic trade deficits nor the distorting effects of chronic trade surpluses. The current reserve system is far from this ideal. Greenwald and Stiglitz propose a reform of the current global reserve system in order to more closely approximate the ideal. They see the primary aims of such reform as alleviating these problems.

The system they propose will do this by 1. decoupling reserve accumulation from the deficit position of any reserve currency countries and 2. providing means of disciplining the surplus countries. This should yield a more stable store of international value than the dollar or any other reserve currency (Greenwald and Stiglitz 2006: 1, 11).

The proposed system rests on the creation of a new currency which Stiglitz (in Stiglitz 2006) names the global greenback. In describing the global greenback, it will be useful to compare similarities and differences with SDRs. Since the proposed Global Greenbacks share many key features with the existing SDRs, the comparison attests to the feasibility of the proposed scheme. Let me begin, then, by describing SDRs.

9.4.1 Special Drawing Rights

Special Drawing Rights or SDRs are currently issued by the IMF. The SDR was created by the IMF in 1969. At the time, the world operated on a fixed exchange rate system. Countries needed public reserves with which to buy their own currency when necessary in order to manipulate the exchange rate and keep it relatively fixed. The key reserve assets were gold and the US\$. However, the international supply of these assets was insufficient to support the expanding volume of international trade and financial development. The SDR was created to fill the role of another reserve alongside these key reserves to cover this gap. However, the fixed exchange rate system soon collapsed and the major economic powers floated their currencies. This lessened the need for SDRs in their initial role as reserves.

Today, they have only limited use as reserves. Their main function is as the unit of account of the IMF and certain other international institutions.

The SDR is not a currency. Nor is it a claim on the IMF. Rather, it *is a potential claim on the freely usable currencies of members of the IMF*. Holders of SDRs can obtain these ordinary currencies in two ways. One, voluntary exchanges between members can be arranged. Two, the IMF can designate members with strong external positions to buy SDRs from members with weak external positions.

The SDR is valued in relation to a basket of currencies – the Yen, the Euro, the Pound Sterling and the US Dollar. The value of the SDR is calculated daily based on the exchange rates of the four currencies in the London market. The composition

and weighting of the currencies in the basket is reviewed every five years. The weightings are revised in the face of changes in the value of the exports of goods and services and the amount of reserves denominated in the respective currencies which are held by other members of the IMF.

The SDRs are allocated in proportion to the IMF subscription quotas. Thus, the majority of the allocation is to a handful of rich Western countries, with the US receiving the single largest share. Allocations of SDR have only been made twice – in 1970-72 and in 1979-81. Countries which have become members of the IMF since that time have not received allocations of SDR.

9.4.2 Global Greenbacks³⁷

The Global Greenback would be a new form of fiat money³⁸. Like the SDR, it will not be a currency which can be used in ordinary transactions. Rather, it is *a potential claim on the freely useable currency of other members* (which *can* be used in ordinary transactions). Under the proposed system, there will be an annual emission of Global Greenbacks. Countries will continue to hold the reserves of gold and of national currencies as they do now, but *additions* to reserves would mostly be in the form of Global Greenbacks.

In the existing reserve system, increases in the world volume of reserves require the reserve country to issue more reserves – that is, to undertake a greater external deficit. The proposed system seeks to loosen the link between accumulation of reserves and the external balance of a country. The annual emission of Global Greenbacks acts as a cushion. In the proposed system, an increase in the world total of reserves does not require a reserve country to issue reserves (by undertaking a deficit). The annual emission is an increase in the world total of reserves. Thus the proposed system avoids the self-undermining characteristic of the existing reserve system in which the ever-expanding supply of the reserve currency continually erodes its value and erodes the confidence of investors, making it decreasingly attractive as a reserve.

The size of the annual emission will be related to the annual aggregate desire for additions to reserves across the world. As we have noted, a component of the desire for increases in reserves is due to the need to keep pace with the increasing volume of international transactions. The general aim of the annual emission would be to increase in proportion to the increasing volume of international transactions. This could be done, for example, by trying to keep the ratio of aggregate volume of reserves in the world to world GDP the same or the ratio of aggregate volume of reserves in the world to aggregate volume of imports in the world the same over time. Here, world GDP and aggregate volume of imports are different indicators or

³⁷ My discussion of Global Greenbacks is based on Greenwald and Stiglitz 2006 and Stiglitz 2006. However, I propose details which are not discussed in those works. The divergences are not because of disagreement with the proposals in those works but rather because I think it necessary to discuss certain issues which are not addressed in the works. The aspects of the proposal may or may not be agreeable to the two authors. As a result, responsibility for the cogency of this proposal ultimately rests with me.

³⁸ Stiglitz 2006 p262 considers a system whereby GG is allocated in exchange for an equivalent amount of national currency. Thus the GG gains its value by dint of the established value of the national currency for which it is exchanged. However, on p 335, Stiglitz adds that, the international monetary authority could just as easily issue fiat money the same way that a central bank can. Here the GG gains value by dint of fiat. I follow this latter possibility.

measures of the volume of international transactions. The choice of ratio will be based on the estimation of the amount by which countries' demand for reserves increases as the volume of international transactions increases.

There are many reasons countries seek trade surpluses. In the existing global reserve system, one of these reasons is in order to make additions to reserves. The idea is that the increase in the volume of international transactions is an important and relatively reliable predictor of the aggregate of countries' desired additions to reserves. Countries may desire to make additions for other reasons as well, but the assumption is that the desired additions due to the volume of international transactions are a good enough approximation to the total desired additions. The annual emission increases the available pool of reserves by approximately the amount needed to meet the desire for additions to reserves.

Of course, external surpluses must still equal external deficits across the world. Countries may still need to borrow money to cover deficits if they simply do not have enough income to pay for their expenses. Also, the aggregate demand for additions to reserves may exceed the amount needed to keep pace with the growing volume of international transactions. The annual emission is a cushion intended to approximate the amount that countries would like to add to their reserves *because of the growing volume of international transactions*. It is not intended to approximate *all* desired additions to reserves.

The value of the Global Greenbacks is this. In emergencies, the country can exchange the global greenbacks for the currency of other members – say, dollars or yen or euro – and use this to mitigate or avoid crisis. The GG is an asset for the holding country because it is a promise that in times of need, it can easily acquire the currency of other countries in exchange for the GG. By becoming part of the GG system, country X also issues a claim on itself – when other countries are in need, they may exchange their holdings of GG for the currency of country X.

Suppose there is an attack on a country's currency. In the existing reserve system, the country would sell hard currency and buy its own currency, as long as it has hard currency in its reserves or can obtain them from the IMF. In the proposed system, the country similarly exchanges Global Greenbacks for conventional hard currencies, whatever they happen to be, and sells them for its own currency.

The exchange rate whereby the Global Greenback is converted to a hard currency could be determined in much the same way as with SDRs. The value of Global Greenback could be set against a weighted basket of currencies of the member countries. The composition of the basket and the relative weightings of the currencies therein could be reviewed periodically.

9.4.3 Allocating Global Greenbacks

The allocation of this amount across countries could be carried out in many ways. For example, it might simply be proportionate to the country's GDP or GDP per capita. I have no rationale for recommending any *specific function* for calculating the allocation. However, I can present a *general rule* for allocation based on the rationale that progressive distribution is desirable. I propose that the allocation depend on per capita GDP, but that countries with lower GDP and lower per capita GDP

receive larger proportional allocations than ones with higher GDP and higher per capita GDP (leaving undefined the specific function mapping GDP and per capita GDP onto size of allocation).

A country which judges its reserves to be insufficient will simply add its allocation of GG to its reserves. A country which is happy with the size of its reserves can move its allocation to its reserves while taking out some hard currency from its reserves. This newly available stock of hard currency can then fund development or poverty alleviation projects. This would be particularly relevant to small poor countries which are in a position of chronic surplus. A smaller economy will need a smaller reserve to meet, say, the prudential guideline. A country in a position of chronic surplus will quite possibly have accumulated a large enough reserve to meet, say, the prudential guideline. A poor country will be allocated more GG than a rich country in the sense indicated in the general rule for allocation I proposed above. Thus, it may well be that such a country does not need much of its allocation to increase its reserves to an acceptable level.

Some countries – especially those with higher GDP and GDP per capita in the ‘progressive allocation’ proposal – may find that their allocation is insufficient to meet their demand for additions to reserves insofar as this is based on the increased volume of international transactions. These countries will simply have to compete over surpluses to augment their reserves.

9.4.4 Disciplining surplus countries

In the existing system, chronic deficit countries with large debts need to achieve sustained surpluses to earn the money to pay off their debts. There are various reasons why these countries find it hard to attain sustained surpluses. For one, they may not have sufficient investment capital or infrastructure or skilled labour or other resources to increase production in a lucrative export market. However, one reason is of particular relevance here as it is inherent in the existing system of settling international payments. In the existing system, chronic surplus countries face no penalty for running surpluses and receive the benefit of greater income and aggregate demand. Thus, they seek to maintain and extend surpluses. Since the distribution of surpluses and deficits around the world is a zero sum affair, this makes it harder for chronic deficit countries to significantly reduce or even reverse their deficits and thus makes it harder to repay debt. Poor deficit countries in particular find that they must divert money from development projects to instead service debt. It is desirable that a new GRS address this issue.

There is a penalty on deficits, namely, having to pay interest on loans to cover the deficit. Here is a way to penalize surplus countries to mirror this. When a country is allocated GG, it could be taxed at, say, 50% per unit of its current account surplus up to the full amount of the country’s allocation (Greenwald and Stiglitz 2006: 12).

Suppose the exchange rate of the currency ‘\$’ to GG is one to one. Suppose country X’s surplus is \$5 and its allocation of GG (based on its increase in volume of international transactions measured by some indicator such as its volume of imports) is GG4. Then, it would receive the GG4, but would have to pay 50% of its current account surplus – 50% of \$5 – to the international monetary authority which

administers Global Greenbacks. If country X's surplus were \$8 or more, it would be taxed \$4 (which is equivalent to its allocation of GG4).

In this scheme, countries which do not have a surplus pay no penalty and thus receive their GG allocation without paying any price in exchange. Of course, countries in deficit face other penalties, such as the cost of drawing down their reserves or borrowing from overseas to cover the deficit. Countries in surplus which receive the GG allocation do pay a price in exchange. This price depends on the size of their surplus. At the limit, the price they pay is equivalent to the allocation they receive. In order to maximize their wealth, surplus countries face the incentive to reduce their surpluses.

If desired, a maximum allowable current account surplus (as a percentage of GDP) could be established which would not be penalized. This would still discourage large surpluses: surpluses above this maximum. At the same time, it would not penalize small surpluses, making it easier for debtor countries to seek chronic surpluses to earn sufficient export revenue with which to service debt. This may not be necessary however, as the allocation of GG to debtor countries can be progressive, allowing them to use some of it to repay debt. Moreover, a country would balance costs and benefits of a surplus in terms of the desire to maximize their wealth from allocations of GG versus the need to service debt through export receipts.

The surplus-tax thus collected by the international monetary authority which administers GG would become a pool of resources for global poverty alleviation. They can be passed to existing agencies with record of competence in particular poverty related areas. As an example, the World Health Organization might be one such candidate when it comes to health. The agency would then dispose of the funds as it sees fit given its expertise (Stiglitz 2006 makes a similar suggestion on p 267).

9.5 Effects of the proposed reforms

9.5.1 Enhanced global economic stability in the proposed Global Reserve System

In the existing global reserve system, the reserve country faces a continuous demand for its currency. As the supply of that currency in the world increases, its value falls. The attendant external debt of the reserve country slowly erodes confidence in its currency. This inevitably makes the currency less attractive as a reserve as it becomes less stable as a store of value.

By contrast, in the proposed system, no country's currency is a reserve and so no country's currency faces this continuous demand. The Global Greenbacks are potential claims on currencies of the members. Only a country can make good on that claim and it can only do so when it faces ongoing or imminent economic crisis (as previously defined by the members of the reserve system). Further, the value of Global Greenbacks is determined by the values of a basket of currencies rather than any single currency, making the value more stable.

In the existing system, the reserve country faces pressure to sustain chronic deficits. These deficits are a deflationary pressure on the economy of the reserve country as the imports are a lag on aggregate demand. Meanwhile other countries face

deflationary pressure as they compete over surpluses so they can accumulate reserves by pushing anyone but themselves into deficit.

In the proposed system, there is no reserve country, and *a fortiori*, no reserve country which faces pressure to sustain chronic deficits. The annual emission of GG creates a buffer which mitigates the severity of competition over surpluses.

For central banks concerned about the stability of the value of their dollar holdings, at the very least, GG offers some diversification. Moreover, it is likely to be much more stable than any single currency, as its value is based on the weighted value of a basket of currencies. Also, as Global Greenbacks reduce the demand for dollar reserves, they reduce the downward pressure on the value of the dollar. Third, the annual emission of GG approximates the annual desired additions to reserves. This will alleviate some pressure of competition to acquire reserves through trade surpluses helping to stabilize international payment and exchange rate dynamics (Greenwald and Stiglitz 2006: 13).

9.5.2 The situation of developing countries in the proposed system

Recall that one of the reasons for holding reserves is as security against global economic instability. Given the increased stability of the global economy under the proposed reserve system (for reasons covered in the preceding section), the volume of reserves needed for this purpose is lower. Developing countries can maintain smaller reserves and divert the money which would otherwise have been piled in reserves to other uses such as development projects and social security nets.

Greater stability also reduces the likelihood of developing countries falling into economic crisis and needing to borrow overseas to stimulate the economy or to pay flighty creditors. This might contribute to lowering the accumulation of debt by poor countries.

In the proposed scheme, deficit countries receive their allocation of GG free. Thus the addition to reserves, in the form of GG, is costless for them. Many poor countries are also chronic deficit countries. These countries benefit considerably from receiving a substantial addition to their reserves free, without the need to divert money from poverty alleviation and development projects.

The proposed system taxes surplus countries and thus penalises surpluses. This provides surplus countries with an incentive to reduce their surpluses in order to receive a larger allocation of GG for their reserves. This makes it easier for poor debtor countries to achieve surpluses and thus repay some of the crippling debt.

The allocation of the annual emission of GG in a progressive manner benefits poor countries. If a poor country does not want to increase its reserves by the amount of its allocation of GG, it can simply withdraw a certain amount of currency from its existing reserves and use that to fund needed projects. Further, the tax on surplus collected by the authority that allocates the GG will be channelled to established aid organisations that undertake projects predominantly for the benefit of poor and developing countries. This addresses a worry that arose in chapter 8 regarding

developing country access to funds in case affordable loans from multi-lateral institutions dry up (see section 8.5.4).

9.5.3 Costs of the proposed system

In the existing system, the US can effectively borrow at will as any issuances of T-bills (a form of debt for the US) readily find buyers desiring additions to their reserves. It can repay the debt by seignorage, printing new US dollars, assured that the desirability of the dollar mitigates the inflationary effect of seignorage. Given the strength of the dollar, the US effectively had a monopoly over issuing paper claims to real goods and services. In the proposed system, the US would lose this ability to borrow large amounts at will and repay by printing money. This might be seen as a large cost to the US.

Britain enjoyed a similar position before the Bretton Woods system, able to print money without a large risk of the Pound losing its value dramatically because of the high demand for the currency. Yet even at the time, Keynes saw it as a mixed blessing. The benefits of seignorage were perhaps more than offset by the adverse consequences of chronic net foreign deficit being a deflationary drag on the British economy. The US has avoided some of these effects by running large and persistent government deficits to sustain full employment. However, this too has potential adverse effects. For one, the government deficit may be funded by the issuance of further debt, which is not a sustainable solution as global confidence in the US economy diminishes.

However, this cost to the US of losing its ability to borrow huge amounts at will is mitigated because of the accompanying benefits. Deflationary pressure on the US economy will be reduced. With less pressure to run current account deficits, the country will find it easier to maintain full employment without such large fiscal deficits. There will also be greater stability in the value of the dollar and less risk of inflation as the money supply need not grow so rapidly. Given these counterbalancing benefits, it is unclear whether the US economy as a whole will be better or worse off.

Conclusion

We began this chapter by noting that the instability of the current global reserve system imposes (i) large opportunity costs on the developing countries as they divert income to reserves to secure against crisis as well as (ii) the cost of the economic crises themselves, which are rendered more likely by the instability.

The model proposed by Greenwald and Stiglitz appears promising as a way to address egalitarian worries (i) and (ii). The proposal seems likely to enhance global economic stability and thus mitigate the above egalitarian worries. In addition, it would make it easier for chronic deficit countries to accumulate surpluses in order to repay their debts, and would create a regular flow of financial aid to poor and developing countries through both the penalty on surplus countries and the progressive allocation of GG. In these ways, the proposed system helps the poor and developing countries. I propose that this model and other contending models be investigated more thoroughly by egalitarians, as possible alternatives to the existing global reserve system.

Chapter 10: Conclusion

Let me list the arguments of my thesis. I began by listing the arguments against the recent egalitarian literature, then presented my novel account in contrast to the literature, ending with a summary of the case study of the various international institutions. I emphasised my divergence from the pursuit of definitive and general philosophical principles that capture our understanding of equality. In this connection, I noted that a characterization of egalitarian political philosophy is more easily available in the form of a growing body of social issues addressed by egalitarians rather than in the form of a substantive ideal or pattern of distribution. This body of work serves to exemplify pressing egalitarian concerns and also to exhibit an egalitarian approach to policies and strategies.

10.1 Existing egalitarian literature

I have argued that the luck egalitarian formulation is inadequate as an understanding of equality. It explains some egalitarian intuitions, but also makes claims that conflict with these intuitions. It might be supposed that the conflicts are with ‘all things considered’ intuitions rather than intuitions about equality *per se* and that the conflicts may vanish if only the latter sort of intuition is considered. However, I have argued that intuitions about equality *per se* are not precise enough to judge the adequacy of the luck egalitarian principle. It might be thought that the LE formulation has advantages for political reasoning and for argument against conservatives that warrant its being chosen as an account of equality. However, I have argued that LE does not play a significant role in identifying social wrongs that concern egalitarians; that it is not uniquely effective against conservative positions; and that it plays no indispensable role in guiding political reasoning in the construction of policies.

I further argued that the existing egalitarian literature implausibly limits itself to considering objections to the distribution of economic product based on states-of-persons. This limitation forms the motivation for engaging in the currency of equality debate, the ‘equality or what’ debate and the intrinsic/instrumental egalitarianism debate.

10.2 The novel account of equality

I presented a novel account of equality that does not attempt to reach beyond egalitarian intuitions. It accepts that egalitarian intuitions are not homogenous and can relate to different themes such as fairness, domination, a concern to meet basic needs, a concern that the interests of some do not receive due priority in the distribution of advantages, and a concern that the disadvantages borne by some are due to factors entirely outside their control. It is a deflationist account because it advances no way to distinguish all and only egalitarian intuitions from progressive intuitions in general.

Acknowledging the diversity of egalitarian intuitions, it is difficult to think of any one way of characterising egalitarianism as a political philosophy. I proposed that a characterisation of egalitarianism is available by applying egalitarian intuitions to various social issues. Such egalitarian investigation aims at diagnosing whether the relevant issues are indeed social wrongs as suggested by egalitarian intuitions about them and, if so, whether egalitarian improvements can be devised and implemented. What is understood by *egalitarianism* as a political philosophy depends on a growing group of social issues for which egalitarians can reach a consensus (more or less) about such matters as: the diagnosis of the main causes of the problems; identification

of mechanisms, institutions, and agents that could improve the situations; and attractive policy proposals. This makes egalitarianism a problem-based approach.

To underline the continuity with the construction of other positions in political philosophy, I noted that other positions can also be discussed as problem-based. The problem of autocracy or dictatorship or monarchy can be mitigated by constitutionalism or republicanism. The problem of inability to voice one's criticisms of powerful institutions is to view freedom of expression as a basic freedom to be protected by the state. Liberalism treats this freedom and various others in this way. The problem of the lack of a significant voice in determining the design or actions of the major institutions that affect one's life chances is the radical democratic suggestion of increasing the channels of democratic control over various institutions and creating new institutions of democratic control.

Insofar as my account presented here does not restrict objections to distribution of economic goods to those based only on states of persons, it is truer to egalitarian intuitions than is the existing egalitarian literature. It also answers the conservative better than the luck egalitarian can. It relates the egalitarian on distributive justice to political philosophy more broadly.

10.3 The case study: global poverty, under-development and the role of certain international institutions

I investigated at length certain social issues from the egalitarian perspective. I looked at the rules of international trade, the institutions of sovereign debt and the global reserve system insofar as they impinge on global poverty and on the development prospects of poor countries. Egalitarian intuitions and social movements have noted the relevance of these institutions to global poverty and development for decades. At the same time, the problems of global poverty and of under-development of the poor countries are among the more pressing problems that confront egalitarians. The choice of this case study thus functioned to present an issue that can properly be said to be of concern to egalitarians, and an issue that is representative of the *central* concerns of egalitarianism (as opposed to an issue which might be a 'hard case' for egalitarian principles but which may not illuminate its core).

Let me summarise some mechanisms that affect global poverty and that can be reformed for progressive ends. The rules governing international trade affect how effectively developing countries can increase their export revenues and domestic employment, expand their industries, diversify their economies, and how easily various infrastructures and institutions are created in their economies. The institutions surrounding sovereign debt affect the level of difficulty a debtor has in paying the debt, the occurrence of over-lending, the opportunity cost to the residents of debtor countries as their governments service debt, and whether residents are held responsible for debt repayments if the debt was not acquired by legitimate rulers. The global reserve system contributes to economic instability, which necessitates the accumulation of larger reserves, or of debt, both as a matter of prudence, and in cases where instability erupts as crisis. Economic crisis itself imposes costs on the poor through greater unemployment, rises in prices of essentials, and lower income.

The egalitarian values relevant to the discussion of these mechanisms include at least the following: fairness; rectifying objectionable international relations imposed by the powerful countries; changing institutions that (whether directly or indirectly) unnecessarily allow external agents to influence a sovereign country's

policy; better prioritising of the interests of the worst off; reducing inequalities due to brute luck and improving the lives of the very poor.

With respect to the rules governing international trade, existing WTO regulations make diversification, development and expansion of exports harder than they need to be for developing countries. I argued that a more progressive system of market access (the MAP) would make these easier. Whilst the MAP would entail some costs for the developed countries, their governments are in a much better position to compensate these costs through productive investment, job creation and safety nets than are the governments of developing countries to take care of their poor in the absence of such a progressive policy.

With respect to the institutions of sovereign debt, the actions of creditor governments and multilateral lenders have contributed to over lending. The absence of sovereign bankruptcy mechanisms has encouraged even greater debt accumulation, and imposed great opportunity costs for the residents of many debtor countries as money spent on debt service could instead have been spent on poverty alleviation programs. Many lenders have lent to despotic rulers, expecting later democratic regimes to continue debt service, and have been aware (or should reasonably be expected to be aware) that the funds would not be spent in the interests of the population. I presented proposals for a sovereign bankruptcy mechanism, and for a mechanism to reduce availability of loans to undemocratic and despotic leaders. Under the sovereign bankruptcy scheme, judgment of a country's ability to service a given level of debt should be sensitive to the social opportunity costs of debt service imposed on poorer residents of the debtor country, and should not be calculated merely in financial terms. I also advocated immediate debt reduction for many countries.

Turning to the global reserve system, I presented arguments that it contributes to global economic instability, and makes it more difficult for chronic trade deficit countries to achieve trade surpluses and thereby earn sufficient export revenue to service debts. I considered a reform proposal that seems promising as a way to reduce the global economic instability associated with the current arrangement, and that would make it easier for chronic deficit countries to achieve surpluses. It would allocate the specially created Global Greenbacks progressively, making it easier for poor countries to accumulate reserves. The progressive allocation, together with the penalty on surplus countries, would be a systematic and unconditional flow of wealth to the global poor, either through their governments or through international and domestic NGOs and multilateral agencies.

The institutions and mechanisms I described are useful markers for any investigation of global poverty. The proposals I considered in my case study require further analysis, especially in terms of their practicability and political feasibility. They must also be compared to other proposed solutions to the same problems. It is only in a reflective equilibrium with social science, current affairs, and real world concerns about practicability, that egalitarian intuitions achieve definition. And it is only in responding to such urgent problems, that egalitarian intuitions find a purpose.

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